INTERNATIONALIZATION

of the Securities Markets

CHAPTER III

Disclosure and Distribution Standards in Relation to Multinational and International Issues of Securities

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CHAPTER III

DISCLOSURE AND DISTRIBUTION STANDARDS IN RELATION TO MULTINATIONAL AND INTERNATIONAL ISSUES OF SECURITIES

I. INTRODUCTION

This chapter of the staff's report centers on issues of importance in the areas of international and multinational finance. The financing techniques described herein are important to all issuers of securities who may turn to the international financial markets in an effort to maximize the returns on their capital-raising activities. The chapter outlines the procedures such persons must follow in order to comply with statutory and regulatory requirements under various legal systems. Legal and regulatory systems in the United States and several foreign countries are discussed, with particular emphasis given the international aspects of securities regulation.

The beginning of the chapter gives an introduction and brief analysis of the international financial markets, distinguishing them from the domestic markets around the world. The international financial markets, while possessing a character of their own and enjoying a relative freedom from domestic regulation, are nevertheless affected by the laws of the countries in which their participants reside. The effects of some of these regulations on the development and growth of the international financial markets are noted. This discussion also includes a description of the international money markets and new evolution of the international capital markets, including the emergence of the Eurobond market, is also analyzed.

Following the discussion of the international marketplace, there is an overview of United States distribution and disclosure practices that affect foreign issuers. Registration provisions for foreign issuers, the use of American depositary receipts, and a brief outline of the statutory liability provisions are included.

The disclosure requirements and distribution practices for securities issued or sold in the European Economic Community and eight major industrialized nations 1/ other than the United States are then set forth. Several EEC Directives relating to efforts toward harmonization of the member states' stock exchange listing regulations and accounting practices are mentioned. The discussion then focuses on the regulatory structure in the eight countries and the nature of their implementing authorities. The major securities markets are identified as are the means by which securities are issued into these markets. Other details of the different securities regulations in these countries are given where relevant.

1/ The countries included in this study are the United Kingdom, Japan, Canada, West Germany, France, Australia, Switzerland, and the Netherlands. Due to time and space limitations, the study of other countries was not undertaken. The inclusion of these countries and the exclusion of others should not be taken to imply any qualitative distinctions, nor are any intended.

The tender offer rules of the United States and several major nations are outlined and compared in a separate section. Finally, some insight into the problems facing issuers and the Commission is provided. In this regard, special emphasis is given to those issues arising in the context of multinational and international distributions and sales of securities.

II. INTERNATIONAL FINANCIAL MARKETS

A. INTRODUCTION

The international financial markets 1/ are vast and complex. They have been characterized as being comprised of many elements, including the Eurosecurities markets; 2/ the foreign securities markets; 3/ the Eurocurrency markets; 4/ the

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1/ These markets are also referred to by some authors as the international securities markets. They are divided into two categories: international money markets, which include short-term instruments, and international capital markets, which include medium- and long-term instruments. These generic terms encompass many subcategories which are used herein to describe more precisely the subject of consideration. *See* Glossary.

2/ Although previously limited to the Eurobond market, this term now includes the recently developing Euroequity market. The prefix "Euro-" is somewhat of a misnomer today. Originally, the market was centered in London and existed throughout Europe. In recent years, however, with the advent of financial deregulation worldwide, the Euromarkets have greatly exceeded their original boundaries, have no national boundaries and are used by borrowers and lenders on a worldwide basis.

3/ This term is used to refer to the various domestic markets in which securities are issued by foreign entities. While Eurosecurities issues are sold internationally by an international syndicate of underwriters, foreign securities offerings are usually denominated in the domestic currency of the country where issued, and are sold primarily within that country by a domestic syndicate. With the advent of financial deregulation, however, these distinctions are becoming increasingly blurred.

foreign exchange markets; 5/ the international financial futures markets; and the syndicated bank credit markets. 6/ While this report is concerned primarily with the Eurosecurities markets, background analysis is made of the Eurocurrency markets since they provide the capital for much of the activity in the securities markets.

1. Scope of Discussion

The discussion begins with a description of the growth and development of the Eurocurrency market. The Eurocurrency market was originally dominated by the dollar sector, commonly referred to as the Eurodollar currency market. These offshore deposits of United States dollars were fueled in the 1960s by several regulatory developments in the United States, as well as by subsequent significant economic developments around the world. The description of the Eurocurrency market is followed

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4/ This is the market for deposit liabilities, denominated in a currency other than that of the country of the bank in which the deposit is made.

5/ This is the international market in which foreign currencies are traded. Transactions in foreign exchange include those in the spot, forward, swap, option and futures markets.

6/ See generally Credit Suisse First Boston Ltd., "The International Capital Markets" (1983) (hereinafter cited as "Credit Suisse").

by a discussion of the international short-term securities markets, referred to as the international money markets.

The international money markets are generally described as including securities issued with a duration of one year or less, as well as loans and other instruments that may not be considered securities. Included in this part of the discussion are descriptions of Eurocommercial paper, which is similar in many respects to United States commercial paper, and Euronote facilities, which provide medium-term financing commitments to borrowers, yet have many of the desired features of short-term borrowing.

A discussion of the international capital markets describes those securities and financing commitments other than Euronote facilities which have a maturity of over one year. The section begins with a historical perspective, focusing first on the development of the Eurobond market, then following its growth and expansion both geographically and in terms of products available therein. Marketing procedures and problems generally applicable to all types of issues of Eurosecurities are described, and disclosure and investor protection concerns are noted. A description of the developing Euroequity market is also included.

Finally, there is a discussion of several of the legal concerns involved in the international or multinational issuance of securities by United States and foreign entities. It is noted that the tax laws as well as the securities laws have a large impact on the terms and conditions of the issuance of these securities. Relevant considerations are pointed out, but discussion of alternatives for resolution of problems now confronting participants in the international markets is deferred to Part VI of this chapter.

2. Introduction to the International Financial Markets

The rise of the international financial markets has been aided by several unrelated historical events. First, the rise of the multinational corporation has increased the need for access to broader capital markets and different forms of currencies. The abolition in the early 1970s of fixed exchange rates has prompted the development of such instruments as currency futures, options and swaps. Similarly, the inflation-generated volatile interest rates of the late 1970s and early 1980s have led to the creation of interest rate futures and swaps. Domestic financial deregulation and the resultant increase in the volume of cross-border capital flows has also contributed to the growth of the international financial markets. Finally, technology advances have greatly facilitated the integration of domestic and international markets.

Because of their enormous size and trading volume, the international markets play a major role in the international flow of capital and have great political, as well as economic, significance. 7/ Borrowers as well as investors have turned to the international markets because of their enormous flexibility, which derives largely from the absence or comparative lack of regulation. Investors are attracted by the large potential marketplace and the wide range of investment vehicles, as well as the anonymity of bearer instruments and freedom from withholding taxes. Other incentives to invest in the international markets are diversification and superior rates of return.

Superior rates of return have been achieved in many foreign equities (as compared to United States equities) since many areas of the world are experiencing higher rates of investment spending and productivity growth than the United States. The primary reason for investing in international bonds, on the other hand, may lie in the array of opportunities and risks provided by the constant shifting of international exchange rate and interest rate relationships. 8/ Portfolio managers seek to capitalize on these shifting patterns and relationships which may provide more investment opportunities

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7/ See generally Fisher, International Bonds (1981) (hereinafter cited as "Fisher").

8/ See Fabozzi & Pollack, The Handbook of Fixed Income Securities (1983) (hereinafter cited as "Fabozzi"), at 637.

than might be available in any single, homogenous domestic market. 9/

International securities of all types may be found to have many similar characteristics, some of which are essential to their marketability. By definition, they are issued in markets other than the domestic market of the borrower. Debt instruments are typically unsecured, although some secured international bonds are issued. Most publicly offered international securities issues are listed on one or more stock exchanges, but are traded almost exclusively in an international over-the-counter market. 10/ Characteristics essential to their marketability include the facts that interest payments are made free of withholding tax at the source, and that the vast majority of equity and debt securities are issued in bearer form.

9/ *Id.,* at 638-43.

10/ This market was originally provided by consortium groups supported by leading European banks. An example of classic cartels, these groups ultimately failed due to the members' own failure to trade exclusively through the groups. *See* Kerr, *History of the Eurobond Market* (1984) (hereinafter cited as "Kerr"). The market today is supported by many market makers, providing deep liquidity in most issues.

B. THE INTERNATIONAL MONEY MARKETS

1. The Eurocurrency Market

The Eurocurrency market exists because of the need for financial intermediation. 11/ United States dollars are by far the most frequently used currency in this market; thus it is often referred to generically (and inaccurately to the extent of all other currency deposits) as the Eurodollar market. 12/ The following discussion focuses on the Eurodollar market; however, it should be noted that the description of that market is similarly applicable to the markets for other major currencies. 13/

11/ International banks are the intermediaries in the system, providing a conduit through which dollars and other currencies may flow from depositors to borrowers.

12/ The size of the Eurocurrency market has grown considerably over the past several years, and as of March 1986 stood at $2,964 billion. This figure represents an increase from $2,386 billion at the end of 1984, and $1,954 billion at the end of 1981. Eurodollar deposits currently represent about 73 percent of the total Eurocurrency market.

13/ It should also be noted that the prefix "Euro-" is an anachronism since foreign currency deposits are not restricted geographically to European banks. Prior to 1968, most of the Eurocurrency market was in fact centered in London. In that year, however, Singapore lifted its withholding tax on interest payments to non-residents, marking the beginning of that city's progression into an important financial center and a

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Eurodollars are deposit liabilities, denominated in United States dollars, of banks located outside the United States, even if the bank is affiliated with a bank whose home office is located within the United States. 14/ Anyone can own a Eurodollar deposit, although such deposits are normally large, involving at least the equivalent of $500,000. 15/ The deposits differ from demand deposits in the United States in that they are time deposits on which interest is paid.

Eurodollars are created when a dollar deposit is transferred from a bank within the United States to a bank outside the country, or when someone outside the United States acquires dollars (e.g.- in a commercial or foreign exchange transaction) and deposits them in a bank located outside the

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(. . . continued)
leading foreign exchange market in the Pacific Basin. Reflecting the geographical separation of the Pacific market from Europe, often the terms "Asiacurrency" or "Asiadollar" are used to describe deposits of foreign currencies in Singapore or other Pacific area international banks.

14/ See discussion in Goodfriend, "Eurodollars," reprinted in Cook & Summers, Instruments of the Money Market (5th ed., 1981) (hereinafter cited as "Goodfriend"), at 123.

15/ See discussion in Eiteman, "International Capital Markets," in Roussakis, International Banking: Principles and Practices (1983), at 60-66.

United States. 16/ In Eurodollar transactions, no dollars actually leave the United States banking system. Rather, foreign banks that accept for deposit and create loans of Eurodollars merely instruct an international bank in the United States at which they have a clearing account to make certain transfers for the credit or debit of described persons. Because hard currency transfers do not occur in the Eurodollar market, the supply of dollars within the United States remains the same, although the size of the Eurodollar market may vary widely depending on deposits made in foreign banks. 17/

16/ For a more detailed description of the mechanics involved in the creation of Eurodollars, *see* Eiteman & Stonehill, *Multinational Business Finance* (4th ed. 1986), at 387-95.

17/ In this connection, it can also be observed that interest rate changes within the United States will always dictate changes in the Eurodollar market, and the converse will never be true. This is illustrated as follows: If the Eurodollar interest rates rose independently, this would cause the volume of Eurodollar deposits to rise. However, the volume of dollars in the United States banking system always remains the same, so a larger spread would result between the United States and Euromarket rates. An oversupply of Eurodollar deposits would then develop since the foreign banks could not loan the dollars competitively, causing the interest rate to return to the original position. On the other hand, if the United States interest rates went up, dollar deposits would flow into the United States banking system, causing the Eurodollar market to shrink, resulting in an interest rate rise in that market.

2. Regulatory Impacts on the Development Of the Eurocurrency Markets

The emergence and rapid growth of the Eurodollar market in the 1960s as a competitor to traditional foreign-exchange banking can be attributed to the regulations placed over on-shore banking operations and the corresponding absence of regulation of off-shore banking centers. 18/ The original rise of London as the center for Eurocurrency dealings was probably due to its historical financial expertise and the widespread use of the pound sterling as an international currency. However, its continued dominance of the market in the face of the recent decline of the United Kingdom's importance in world trade and the corresponding decline in the use of sterling for finance has probably been due to the significant absence of regulation by the United Kingdom of offshore transactions in foreign currencies. 19/

The Eurodollar market has continued to flourish largely due to the absence of certain types of regulation over the banks that participate. In most countries where banks are active in the Eurodollar market, there are no requirements to

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18/ *See generally* McKinnon, "The Eurocurrency Market," *in* Princeton University, *Essays in International Finance* (No. 125, Dec. 1977).

19/ *Id.*, at 6-7.

maintain non-interest bearing reserves, no government-mandated insurance requirements and few, if any, artificially imposed interest rate restrictions. Should a local government impose such requirements or regulations, the market would merely shift to another country.

Although there is usually a higher rate of return on Eurodollar deposits than on United States dollar deposits, there is also a perceived risk differential, commonly referred to as the "London premium." This risk involves the lack of insurance coverage on the deposits and the absence of a national central bank standing expressly behind the banks to provide liquidity in a crisis. Another element of the London premium involves perceived political risks. 20/

Regulatory restraints on the United States banking community during the 1960s involving restrictions on the flow of both long-term and short-term capital and interest ceilings greatly increased the growth of the Eurodollar market. 21/ Capital controls within the United States forced corporations in this country to go into the Euromarket to borrow funds,

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20/ *See* Goodfriend, *supra* n.10, at 128-32.

21/ These included the Interest Equalization Tax of 1964, retroactive to 1963; limitations imposed in 1965 on acquisition of foreign assets by United States commercial banks; the requirement in 1968 that United States multinational corporations raise funds outside the United States for new direct foreign investment; and the interest rate ceilings imposed by old Regulation Q.

largely for investment abroad. 22/ While these restraints now have been largely removed, the Euromarket is well-established, and remaining regulations, such as reserve and insurance requirements, are sufficient to perpetuate the demand for Eurodollars.

The continued existence and vitality of the Eurodollar market has provided the impetus for the development of the Eurobond market as well. Part of the reason for this is the availability outside the United States of sufficient dollars to supply a considerable demand by borrowers. Thus, borrowers wishing to avoid United States regulatory barriers but desiring to obtain United States dollars rather than another currency may issue bonds in the Euromarket. This allows borrowers to avail themselves of the huge pools of dollars that exist outside the regulatory control of the United States and is an important reason for the proliferation of the Eurobond market today.

While no fundamental changes in the regulation of the Eurodollar market appear imminent, a debate has taken place recently over whether some regulation is appropriate. There are three basic issues underlying this debate. The first issue concerns whether the Eurocurrency market has contributed to

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22/ The viewpoint in the United States at that time was that the balance of payments deficit required funds to be raised abroad for direct foreign investment purposes rather than permitting the use of scarce domestic capital resources.

worldwide inflation by complicating monetary control and providing a too ready source of capital. The second issue involves whether the Eurocurrency markets have contributed to exchange rate instability. Finally, there is a question of the degree of safety of the system of Eurobanking operations. 23/

3. Today's International Money Markets

a. Eurocommercial Paper

The advent of the Eurocommercial paper market is a recent occurrence, unlike the United States commercial paper market, which has been in existence since the 19th century. 24/ Commercial paper is short-term, unsecured debt issued in the

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23/ For a discussion of these and other regulatory issues, see Frydl, "The Debate over Regulating the Eurocurrency Markets," 1979-80 FRBNY Quarterly Review 11 (Winter 1979-80); Greenburg, "The Eurodollar Market: The Case for Disclosure," 71 Cal. L. Rev. 1492 (1983).

24/ The Eurocommercial paper market is, like its counterpart in the United States, a market for short-term unsecured debt instruments issued by large, well-known corporations. The market provides an alternative financing vehicle in the Euromarket to short-term bank loans. Eurocommercial paper is usually sold at a discount to large institutional investors, but the market differs from the United States domestic commercial paper market in that it is much smaller due to its recent development.

form of promissory notes. 25/ The sale of commercial paper is basically a substitute for short-term bank loans, and was originally necessary in the United States due to restrictions that prevented banks from providing service in more than one state. The advent of consumer finance companies at the beginning of this century also contributed to the growth of the

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25/ Most of this paper is of 270 days duration or less. Longer term commercial paper must be registered with the Commission since it is not exempt under Securities Act section 3(a)(3). Most domestic and Eurocommercial paper is issued under the section 3(a)(3) exemption, although section 4(2) has also been used for issues of commercial paper that either have maturities exceeding statutory requirements or have other characteristics that would cause them to fall without the parameters of section 3(a)(3) (e.g., notes not intended for use to finance current transactions).

Commercial paper is sold on the open market, either in interest bearing form or, more frequently, on a discounted basis. As of 1985, more than 1,300 companies in the United States were issuers of commercial paper, with financial companies comprising more than 70 percent of the market. Federal Reserve Bank of New York, Commercial Paper (1985), at 1. Commercial paper is distributed through dealers or directly through finance companies. Industrial companies and some consumer finance companies use dealers to place their commercial paper with investors. A very competitive marketplace and resultant small spreads dictate that commercial paper be sold only in large increments, usually no smaller than $250,000. Smaller increments may be found in the direct commercial paper market, which is used by finance companies who are able to place their paper directly with investors. These institutions may be more willing to issue paper in smaller denominations to facilitate investment by a greater number of individual investors. Further, the usual dealer spread of about 1/8 of a percentage point, or $125,000 on every $100 million placed, can be saved through direct issuance.

United States commercial paper market because of the need for capital to lend directly to consumers. In the past forty years, the long upward trend in interest rates and the huge increases in sales of financed consumer goods have caused a great expansion in the United States commercial paper market. 26/

Prior to the early 1970s (and to a large extent throughout the 1970s and early 1980s), the United States market was used to satisfy the commercial paper needs of both United States and foreign private and sovereign issuers. The first Eurocommercial paper issue, by the Aluminium Company of America, was brought to market in 1970 by the predecessor of Credit Suisse First Boston Limited. 27/ The idea did not encounter widespread acceptance by European issuers, however, and the market became inactive until the early 1980s. Several United States issuers returned to the market in 1980, and in 1981 the first non-United States issuer, the Marubeni Corporation, entered the Eurocommercial paper market.

This market has risen rapidly over the past five years, with further increases anticipated. One reason for the rise of the Eurocommercial paper market may be the advent of flexible

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26/ For a discussion of the history and development of this market, as well as issuing techniques and investment considerations, _see_ Fabozzi, _supra_ n.7, at 232-42.

27/ _See_ Credit Suisse, _supra_ n.4.

framework agreements that allow an issuer to request immediate sale by a dealer, or under which a dealer may take advantage of a market window by requesting the issuer to sell paper. Another factor in the growth of the Eurocommercial paper market has been the rise in telecommunications capabilities, which has created a marketplace in which every minute is crucial. Thus, in a market where timing is of utmost importance, the fact that the European markets open sooner in the day than the United States markets has contributed to the growth of the Eurocommercial paper market.

The use of Eurocommercial paper by blue chip issuers has become an attractive alternative to bank borrowing recently due to the development of the Eurocommercial paper market. The borrowing rate is usually set at a small margin above that for bank money market securities of similar maturities (which in turn is slightly less than the London interbank market and the United States commercial bank market). It is also desirable as a means for diversification of an issuer's source of funds.

Unofficial figures 28/ set the value of today's United States commercial paper market at $253 billion outstanding, as compared with the $58 billion value of Eurocommercial paper

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28/ These figures were supplied by panel speakers at the Biennial Conference of the International Bar Association, Section on Business Law, Committee on Issues and Trading in Securities, September 16, 1986, New York.

outstanding. 29/ Several differences are inherent between the United States and Eurocommercial paper markets. The United States borrowing instrument is typically a simple promissory note, usually governed by New York law. The notes issued in Eurocommercial paper financings are more complex. United States commercial paper is usually backed by a letter of credit or other guarantee, while the European counterpart has no such credit enhancement. In order to achieve market acceptance in the United States, it is necessary that issuers of commercial paper have an investment grade rating by one or more rating agencies. 30/ This has not been a requirement in the Eurocommercial paper market, however, possibly due to the lack of comparable rating agencies in most other countries. 31/

29/ Investors in the Eurocommercial paper market include private pension funds, money market mutual funds, governmental units, bank trust departments, foreign banks and investment companies.

30/ The following five organizations currently rate commercial paper: Standard and Poor's, Inc. and Moody's Investor's Services each rate more than 1,300 issuers; McCarthy, Crisanti, Maffei, Inc. rates more than 500 issuers; Fitch Investor Services Corp. rates more than 240 issuers; and Duff and Phelps, Inc. rates more than 100 issuers.

31/ This distinction can cause a marketing problem for some United States investors. For example, many United States institutional investors are restricted in their securities purchases or investments to instruments that are of a certain investment quality. For a discussion of EuroRatings, the new London-based European rating agency that has recently commenced operations with the issuance of ratings on short- and

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Nevertheless, there are currently about six United Kingdom issuers that have been rated by Moody's. 32/ Other distinctions between the two markets involve different lengths of maturities 33/ and the forms in which the securities are issued. 34/ Finally, United States commercial paper issues typically are done on a firm underwriting commitment basis,

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long-term debt of 45 foreign issuers, see Part IV.B.8., infra. See also individual country chapters for discussions of their domestic rating agencies.

32/ There is some reluctance by European issuers to submit to the rating process by United States credit agencies. For instance, there would be considerable embarrassment if the company did not receive the rating that it desired or expected. Further, the rating agencies look closely at many aspects of the business of the issuer, including its liquidity, and the procurement of a rating involves certain fixed costs. Since one of the principal reasons for issuing commercial paper in the Euromarket is cost, the additional fees involved in obtaining a rating may affect the decision to enter this market.

33/ United States commercial paper maturities vary over a broad range, from 25 to 270 days. Eurocommercial paper is usually issued in maturities of six months. Issues of Eurocommercial paper by United States companies are limited to maturities of 183 days or less in order to take advantage of the exemption from United States withholding tax for certain short-term discount obligations.

34/ United States commercial paper is usually issued in physical form, while Eurocommercial paper is increasingly being issued in paperless form, with most trades cleared on the books of one of the clearing agencies set up to service the Euromarket.

while Eurocommercial paper offerings are usually brought to market on a best-efforts basis.

b. Euronotes: Innovative Medium Term Finance

The recent development of medium-term Euronote issuing facilities 35/ demonstrates the scope of financial innovation that this largely unregulated market continues to experience. In order to understand the need for these note facilities, it is useful to refer briefly to the sources of medium-term credit utilized over the past two decades.

In the 1970s, short- and medium-term credit facilities were provided almost exclusively in the Euromarket through Eurocredits. Eurocredits are lending facilities set up by bank syndicates that can be drawn upon under certain circumstances by the borrowers. Problem loans that surfaced late in the

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35/ Euronote facilities take many forms, as discussed in this section, but can be characterized generally as a method whereby companies arrange to sell short-term notes (comparable to commercial paper) from time to time in international markets. The facilities provide that the notes will be purchased by the underwriters in the event that they cannot be successfully placed with investors. Such facilities entail two types of risk, borne separately by the underwriters and the company. Risk of market fluctuations is borne by the underwriters since they ensure that the notes will be purchased, while risks specific to the issuer are borne by the issuer since the underwriters are promised that the agreement may be avoided in the case of an adverse event affecting the issuer's credit.

1970s and early in the 1980s caused such bank syndicates to acquire a profound distaste for such facilities and the detrimental effect they had on balance sheets. Thus, the Eurocredit of the 1970s slowly became replaced by new financing instruments that are commonly used in the 1980s. These new instruments include floating rate notes (FRNs) for long-term capitalization, Euronotes for medium-term debt, 36/ and Eurocommercial paper for short-term liquidity.

Euronote facilities are designed to blend the short-term nature of Eurocommercial paper with the need of borrowers for medium-term financing commitments. In fact, there are very few differences in the notes issued under a Euronote facility and Eurocommercial paper, other than that the former are issued pursuant to an agreement which is designed to keep available a certain amount of the issuer's paper for a stated period of time (medium-term). 37/ Euronote facilities may be provided on either an "end-to-end" or "revolving" basis. In the former case, a set amount of notes is constantly outstanding

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36/ For a comprehensive discussion of today's Euronote market, *see* Bankson & Lee, *Euronotes* (1985).

37/ Other differences are a result of the fees charged to establish and maintain the facility and the corresponding slightly higher interest rate that must be charged. Fees charged include the facility fee (usually 3-15 basis points), a utilization fee (5-10 basis points), a management fee (5-15 basis points), and a variable commitment fee for unused portions of the facility.

throughout the term of the facility, and is merely rolled over by the underwriters. A revolving facility, by contrast, has a maximum amount that may be drawn down by the issuer at its convenience, and the amount outstanding may vary significantly over the term of the facility. 38/ Such facilities are attractive to banks since the obligation to place notes is not reflected on their balance sheets. 39/

The intense competition in this market has led to a proliferation of names and types of Euronote facilities. The two most well-known are the RUF and the NIF. A RUF, or revolving underwriting facility, combines an arrangement for issuing short-term notes with a medium-term commitment from a group of international banks to purchase the notes if they are not sold immediately to investors. The acronym NIF, which stands for note issuance facility, identifies a facility similar to a RUF, but may be used to describe a situation where

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38/ The Euronote facility is usually an arrangement among the issuer, the arranger or manager of the facility, and the group of banks that provides the commitment to purchase the notes. A more detailed description of the roles of the various parties may be found in Whitman, "Short-Term Euronote Facilities, Revolving Underwriting Facilities, and Euro Commercial Paper," *in* Practising Law Institute, *Current Corporate Financing Techniques* (1986) (hereinafter cited as "Whitman"), at 301-02.

39/ Since these facilities are contingent contractual duties, they are not classified as assets, which must be recorded on banks' balance sheets.

only a best-efforts type commitment is made to the borrower. 40/ Other acronyms have been given to Euronote facilities in an attempt to distinguish them for marketing purposes. 41/

Euronote facilities may be underwritten through a sole placing agent or through what is known as a "tender panel" facility. In the case of the former, if the placing agent is unable to sell the paper in the market, the underwriting banks must each purchase a portion of the issue at the facility price. This arrangement was unsatisfactory to many banks; thus, the tender panel was created, whereby the underwriters may bid for notes of the issuer upon its request. The issuer can then accept the bids in order of the lower yields.

Purchasers of Euronotes tend to be sophisticated investors

40/ Whitman, supra n.37, at 287.

41/ An illustrative, but certainly not exhaustive, list includes the following: TRUF, or transferable revolving underwriting facility (provisions for relatively easy transfer of rights and obligations under the facility); PUF, or prime underwriting facility (based on the United States prime rate instead of the usual LIBOR, for less credit-worthy borrowers); SNIF, or syndicated (or standby) note issuance facility; MOF, or multiple option facility (providing for financing of several types, e.g.- commercial paper, bankers' acceptances, etc.); and GNF, or global note facility (allows issuance of commercial paper in both Euro- and United States markets according to windows of opportunity).

who desire the liquidity of money market instruments. 42/ The credit-worthiness of the issuers will dictate the interest rates available to them, which in turn will attract different types of investors. Less developed countries and smaller, lesser known companies will generally obtain credit in the LIBOR+ range, 43/ attracting commercial banks as investors. Developed countries may issue notes bearing interest in the LIBID 44/ range (or even below LIBID), attracting large institutions and pension funds as investors. A LIMID 45/ range is usually available to multinational corporations, and a broad range of investors including those listed above have exhibited an interest in these notes.

An information memorandum is used as the disclosure and selling document for Euronotes issued pursuant to a note issuance facility. The memorandum has derived some of its characteristics from documents used in international syndicated loans, United States commercial paper offerings, and typical

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42/ There is an active secondary market in Eurocommercial paper and Euronotes, even though many investors hold the notes to maturity.

43/ London interbank offered rate. LIBOR is the deposit rate applicable to interbank loans within London.

44/ The term refers to the London interbank bid rate.

45/ The term refers to the mid-range of the spread between LIBID and LIBOR.

Eurobond issues. However, the format has been structured to address the lengthy commitment period, the continuous offering nature of the facilities, and the sophistication of the potential investors. Thus, the information memorandum typically contains two parts: first, "facility specific" material which describes the terms of the particular issue; and second, a description of the borrower, usually including (or incorporating by reference) the most recent annual audited financial statements and all subsequent interim or special reports. 46/

c. Other Products

Other money market instruments are gradually being used more frequently in the Euromarket. 47/ Among these are certificates of deposit ("CDs"), which were first introduced to the Euromarket in the early 1960s by leading United States commercial banks. An active secondary market has developed for CDs issued in the Euromarket. While United States banks are subject to reserve and other regulatory restrictions, their European branches and foreign competitors are not. Thus, more

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46/ *See* Whitman, *supra* n.37, at 306-07.

47/ *See generally* Fabozzi, *supra* n.7, at 665-70.

favorable rates may be obtained in the Euromarket for these instruments.

Some London banks have begun to issue CDs denominated in pounds sterling. CDs have also been issued in floating rate form, with the applicable interest rate keyed to LIBOR or, in the case of Asian-dollar CDs, the Singapore Interbank Offered Rate (SIBOR). 48/

Another type of money market instrument available in the Euromarket is the bankers' acceptance. This is a draft for payment of United States dollars by a United States bank that has been accepted by that bank. Such bills are traded actively in a secondary market on a discount basis and are not subject to United States withholding tax. In London, these instruments are called banks bills, and are highly liquid instruments. 49/

48/ SIBOR is the deposit rate applicable to interbank loans in Singapore.

49/ *Id.*, at 666-67.

C. THE INTERNATIONAL CAPITAL MARKETS 50/

1. Historical Perspective

The largely unregulated international capital markets provide mechanisms through which individuals and non-banking institutions are able to participate in highly diversified financial investment vehicles. The fiercely competitive nature of this market has fostered the proliferation of financial products and techniques never before utilized in traditional domestic markets.

The beginning of the Eurobond market can be traced back to 1963, to an issue by Autostrade. 51/ The year 1963 is significant also for United States issuers because that was the retroactive effective date of the Interest Equalization Tax of

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50/ The term "international capital markets" includes both domestic issues of securities by foreign companies in the domestic currency (foreign bonds) as well as multinational offerings not necessarily denominated in the currency of any of the countries involved (Eurobonds). Only the latter type of security will be discussed herein. *See* discussion at notes 1-3, *supra.*

51/ Autostrade is the operator of toll roadways in Italy. The issue was guaranteed by IRI, a state-owned holding company. The lead manager of the $15 million, 15-year financing was a London bank, while the co-management group included banks in Belgium, West Germany, the Netherlands and Luxembourg. *See* Fisher, *supra* n.6, at 19-20; Kerr, *supra* n.5, at 11-16.

1964 (the "IET"). 52/ The IET was the Kennedy administration's response to the perceived contribution of foreign issues of securities in the United States market to the United States' balance of payments deficit that existed at that time. Foreign issues were typically offered at a more attractive interest rate than domestic issues, resulting in a large capital outflow. The IET was designed to effectively reduce the yield on foreign securities to United States investors, thereby making them less attractive. Imposition of this tax caused foreign borrowers to turn to foreign markets to obtain capital. The huge pool of dollars contained in Eurodollar deposits in international banks was the best available source for dollars outside the United States, and the Eurobond market developed in order to take advantage of this capital base.

Although the IET did not cure the United States' balance of payments problem, it had the collateral effect of encouraging the reopening and development of European capital markets. The entry of United States corporations into the Euromarket accelerated in 1965 with the imposition of voluntary restraints on capital formation by multinational corporations.

52/ The IET imposed a tax on issues by foreign entities of securities in the United States. The idea of "equalization" derives from the fact that prior to the tax, issuers of foreign securities in the United States could offer a higher yield on the securities than could comparable United States issuers due to interest rate differentials between the United States and foreign markets.

The voluntary restraints promoted capital formation abroad by United States corporations by requiring them to finance their foreign operations from abroad. The change in 1968 in the program from voluntary to mandatory and the creation of the Office of Foreign Direct Investment to administer the controls caused an immediate surge in the volume of dollar-denominated Eurobonds issued by United States corporations during the late 1960s. 53/

The mid-1970s saw several further developments in the Eurobond markets. In 1974, the IET was allowed to expire, causing speculation that the Eurobond market would soon be displaced by the United States domestic market. This never happened, however, and the Eurobond market continues to flourish. In 1977, the European Investment Bank floated the first Euroyen bond issue. Since that time, Euroyen bond issues have become increasingly important due to significant regulatory developments in both the United States and Japan that have simplified procedures for issuing Eurobonds by United States and Japanese companies. In 1984, Japan first allowed Japanese companies to issue yen-denominated bonds outside

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53/ The volume of Eurobond issues by United States companies increased from $527 million in 1967 to $1,963 million in 1968. The years during which the Mandatory Restraint Program was in effect (1968 through 1973) saw United States corporations float 271 Eurobond issues for a total of $6,978 million, or nearly 33 percent of the entire market over the period. Fisher, supra n.6, at 21.

Japan. The next year saw the removal by the Japanese government of the 20 percent withholding tax on interest paid to foreign securities holders by Japanese companies. These developments have allowed Japanese companies to access the cheaper capital that is available in the Euromarket, and to structure borrowings that are not secured, which are typical in the Euromarket but rare in Japan.

In the United States, the passage of the Tax Reform Act of 1984 ("TRA 1984") facilitated Eurobond financings by United States issuers by repealing the 30 percent withholding tax on payments of "portfolio interest" in the case of debt securities issued after July 18, 1984, to non-United States holders. 54/

The creation of central clearing houses for different types of Eurosecurities has also facilitated the growth of

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54/ Prior to that time, a convoluted structure was necessary for the issuance of Eurobonds by United States companies in order to avoid the withholding tax. The United States corporation would set up an off-shore single-purpose finance subsidiary that would issue bonds into the Euromarket. For marketing purposes, the bonds would be guaranteed as to principal and interest payments by the parent company. After closing, the subsidiary would loan the proceeds of the offering to the parent. The interest payments by the parent to the subsidiary would not be subject to withholding tax due to a tax treaty between the United States and the offshore jurisdiction where the finance company is incorporated.

For a further discussion of Eurobond tax considerations, see Beller & Berney, "Eurobonds," 19 Rev. Sec. & Commodities Reg. 39 (1986); discussion at Part C.5.a., "Tax Law Considerations," infra.

markets for those securities. Originally established to provide for easy clearing, storage and transfer of Eurobonds, Euro-clear 55/ and Cedel 56/ have evolved into international clearing houses for many types of securities. These institutions are subject to the regulations of the Association of International Bond Dealers, a self-regulatory organization of international importance.

2. Bringing a Eurobond Deal to Market: Procedural Aspects

a. Marketing Considerations

Two distinguishing characteristics of most Eurobonds are that they are issued in bearer form and interest is paid free of withholding taxes. Recently, the former requirement has been eroded because institutional purchasers are replacing individual investors in the Eurobond market, and institutions do not have the same perceived need for anonymity as do wealthy

55/ Established in Brussels in 1968 by Morgan Guaranty Trust Co., Euro-clear is owned by a large number of mostly European and North American banks. *See* Kerr, *supra* n.5, at 98-100.

56/ Established in Luxembourg in 1971 to provide competition for Euro-clear, Cedel is owned by a large group of European banks.

individual purchasers. 57/ The Eurobond market can be characterized as a "name market," i.e., well-known issuers from developed countries dominate the market, which is by its nature very conservative. 58/ International banks that bring these issuers to market are reluctant to underwrite securities of financially nominal or lesser-known issuers, because they will suffer harm to their reputation that may affect their ability to obtain future business if problems surface with the deals. 59/ Other essential factors that may affect a company's

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57/ The greatly increased role of institutional investors in the United States domestic market has been mirrored in the Euromarket. Among the most active institutional investors in the Euromarket today are such entities as central banks, especially of oil-producing countries which have accumulated enormous reserves over the past decade (so-called "petrodollars"). Other categories of institutional investors include government agencies and international organizations, pension funds, insurance funds, investment companies and trusts, corporations and bank trust departments. See, e.g., Fisher, supra n.6, at 31-32.

58/ Since foreign issuers are generally not rated by United States credit agencies, the names and reputations of both the borrower and the underwriters are very important to the marketability of the issue.

59/ This is not to say that such issuers are not brought to market. Relatively smaller banks may be more willing to underwrite lesser-known issuers' securities in an effort to develop a client base and exhibit placing capability, both of which will help them edge into the underwriting groups for the better-known issuers, which will typically be led by the largest banks.

acceptance in the marketplace are its size and past issuing frequency.

The lack of a disproportionate number of failures in this market as compared to more regulated markets may be attributed to several factors, including the reluctance of banks to do business with lesser-known or smaller companies. 60/ In recent Congressional hearings, several industry leaders commented that despite large regulatory differences between the United States market and the Eurobond market, there have been no significant failures of financial institutions in the Eurobond market. 61/

As a result of the intense competition in the Euromarket, many product innovations recently have been introduced. By far

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60/ Generally, United States companies rated below the level of single A have difficulty arranging financing in the Euromarket. Thus, new and emerging ventures have very restricted access to the market, and in any event, the participation of a major bank in a deal is essential to its acceptance by the market. *See* Von Clemm, "United States Companies Raising Capital Abroad," 1981 J. Comp. Corp. L. & Sec. Reg. 122, at 129.

61/ *See* *The Internationalization of Capital Markets: Hearings Before the Senate Comm. on Banking, Housing, and Urban Affairs,* 99th Cong., 2d Sess. (1986) (responses to written questions from Senator Garn). The impression of the participants was that such differences had no impact on financial institution failures due in part to their professional nature. Although there have been international financial institution failures, these have been a result of reasons other than their participation in the Eurobond market. *Id.,* at 150, 161, 205, and 228. *But see* discussion regarding Investor Overseas Services *in* Kerr, *supra* n.5, at 32-34.

the most successful new product has been the floating rate note ("FRN "). 62/ These are particularly attractive to institutional investors today, since interest rates are keyed to LIBOR. FRNs now constitute at least a third of all issues done in the Eurobond market. The coupon in these issues is reset every three to six months, subject to a set minimum. FRNs have now been coupled with other innovative features such as put options and procedures whereby the rate may become fixed for the remaining maturity of the note. 63/

Examples of other recent innovative products are oil-indexed bonds, zero coupon bonds, deferred coupon bonds, warrants, extendible notes, multi-currency instruments and deep discount bonds. Foreign currency denominated bonds have become popular with United States issuers over the past few years. These bonds provide an opportunity for arbitrage in the foreign exchange markets. This opportunity, when coupled with the development of the huge currency swap market, decreases the

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62/ FRNs were actually created in 1970 with an issue by Ente Nazionale per l'Energia Ellectrica (ENEL), the government-owned Italian power company; however, their use has greatly increased recently, especially with banks as issuers. For an interesting discussion of claims by several individuals to first having the idea of creating floating rate notes, _see_ Kerr, _supra_ n.5, at 36-38.

63/ The 1979 issue by TVO Power Company was called a Floating Rate Drop-Lock. This set a minimum beyond which the rate could not descend, and provided that if the rate actually reached this point, it would be locked into that rate until maturity.

costs of borrowing in the Eurobond market. There are basically two types of foreign currency denominated bonds used: the single currency or the dual currency. One example of a dual currency offering provides that the issue price and interest are payable in a foreign currency, while the principal is payable in another. 64/

b. Organization and Timing

The structure of the typical Eurobond syndicate 65/ is somewhat different from that commonly used in the United States in that it encompasses three tiers as opposed to the two-tier

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64/ Recent issues have been floated by Student Loan Marketing Association and Federal National Mortgage Association, both in yen and dollars.

65/ The Eurobond syndicate framework typically is the same as that commonly utilized in the United Kingdom. *See* discussion in Part IV, *infra.* United Kingdom merchant banks, together with United States investment banks, led the field in the 1960s, joined in the 1970s by large Swiss and German banks. The Japanese have made significant inroads into the Euromarket underwriting business in the 1980s. Creative issuing techniques are also being introduced. These include the "bought deal," which seeks to avoid the negative effects of the grey market discussed *infra* at n.67. In the bought deal, one or two banks buy the entire issue from the borrower, then try to place it immediately in the market. Naturally, such banks must have significant capital reserves to accommodate this type of commitment, and substantial market risks are involved.

arrangements found in this country. 66/ The first tier consists of the management group, the second includes the underwriters, and in the third tier are found the selling group members. The managers are usually contractually committed to purchase the entire issue from the borrower, while the underwriters are contractually committed to purchase certain portions of the issue from the lead managers. In the United States, typically the underwriters are all committed to purchase the issue from the borrower. Selling group members purchase their allotted portions of the offering directly from the managers in the Eurobond issue, as opposed to purchasing from the underwriters in the United States issue.

There are several significant days that occur in the process of bringing an issue of Eurobonds to market. The first is the announcement day, which usually takes place a week or two before the actual offering commences. At the announcement, the issuer, amount, maturity and coupon of the projected issue are announced. Following the announcement day, and prior to the offering day, is the subscription or offering period. It is during this time that the selling group is formed and underwriting commitments are finalized. 67/ Preliminary

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66/ *See* discussion in Part III, *infra.*

67/ During this time there is generated a so-called "grey market" in the securities. This market is a sort of "when-issued" market, and can have a significant effect on the price of the issue. Prohibited by

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offering documents, consisting either of a prospectus or offering circular, are distributed at this time. Also during the subscription period the issuer applies to an appropriate exchange for listing.

The next significant event is the pricing of the issue. Since the maturity and coupon have already been announced, the market has had time to respond to the terms of the issue. This results in a determination by the lead managers of the appropriate issue price on the day (or night before) the offering commences. After the offering agreement has been signed, allotment telexes are sent to the various underwriters and selling group members indicating their individual portions of the offering. Closing of the deal, including payment to the

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United States securities laws in this country, the grey market occurs in connection with Eurobond issues when members of the selling group and underwriters are subjected to pressure from purchasing institutions to supply the issue at discount rates prior to the actual offering date. This can be done by estimation of the actual offering price and subtraction from that of some or even all of the underwriting and selling commissions to be received. Naturally, such practices cause downward pressure on the ultimate issue price, and lead managers do not look favorably on underwriters or selling group members discovered to be participating. For further discussion of the grey market and its implications, _see_ Fisher, _supra_ n.6, at 80-82. Nevertheless, the grey market has become an accepted part of the Euromarket today, and arguably performs an important function in pricing efficiency. _See_ Kerr, _supra_ n.5, at 56-57, 88-89.

issuer of the funds generated thereby, usually occurs within two weeks of the offering day.

3. Disclosure and Investor Protection

One reason commonly cited for the growth of the Eurobond market is the lack of direct regulation over it by any national government, which allows an environment of free competition. Despite this unregulated atmosphere, disclosure is provided according to market requirements, and the lack of uniform disclosure guidelines has not resulted in a disproportionate number of defaults or failures of financial institutions in the market. Nevertheless, each participant in the Euromarket is necessarily resident in some country, and each country has some form of securities regulation which affects practices in the international marketplace. Since virtually all Eurobond and Euroequity offerings are listed on an exchange, 68/ the disclosure requirements of the country in which the exchange is located must be followed. Further, currency restrictions in most countries affect participation by their nationals in the Euromarket as well as the use of their currencies in international finance.

68/ This is done for the purpose of, among others, satisfying the needs of institutional investors who may be restricted by their domestic authorities as to the types of investments that they may acquire and hold.

Effective national disclosure requirements such as those in the United States have arguably contributed indirectly, but significantly, to the disclosure standards in the Euromarket. The existence and impact of United States regulation on the United States market, which is the largest securities market in the world, have caused the international marketplace to come to expect certain information to be provided regardless of whether it is required by law. In addition, the European Economic Community has adopted certain Directives in an effort to set forth minimum statutory requirements regarding corporations, listing requirements for exchanges and continuing disclosure. 69/ Many countries in Europe currently have domestic disclosure requirements more comprehensive than the standards set forth as minimal requirements in the Directives. However, some countries have segregated disclosure requirements for issues that are done other than simply within the domestic market. An example of this is found in the listing

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69/ *See, e.g.,* Council Directive of 5 March 1979 coordinating the conditions for the admission of securities to official stock exchange listing, 22 O.J. Eur. Comm. (No. L 66) 21 (1979); Council Directive of 17 March 1980 coordinating the requirements for the drawing up, scrutiny and distribution of the listing particulars to be published for the admission of securities to official stock exchange listing, 23 O.J. Eur. Comm. (No. L 100) 1 (1980); Council Directive of 15 February 1982 on information to be published on a regular basis by companies the shares of which have been admitted to official stock-exchange listing, 25 O.J. Eur. Comm. (No. L 48) 26 (1982). *See* discussion at Part IV.A., *infra.*

requirements for the International Stock Exchange. 70/ There are special provisions applicable solely to offerings in the Euromarket which, among other things, provide for less stringent disclosure requirements.

Thus, in the Euromarket, while no comprehensive, single set of rules delineates precise disclosure requirements, as a practical matter, the prospectuses and offering memoranda used to sell securities there are sufficiently detailed, in most cases, to provide all necessary information 71/ to investors. Although there have been examples of failures of this disclosure system, 72/ these are few compared to the volume of successful issues. It therefore appears that a combination of

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70/ London Stock Exchange, Admission of Securities to Listing (1980), at Section 7.

71/ The term "necessary information" is used in this context to describe the concept of that information which is required by the investor according to its demands before it will invest. This concept assumes the investor will not buy securities about which it does not have sufficient information - an assumption essential in understanding the market forces that shape conduct in the Euromarket. As noted earlier, since the Euromarket is largely a "name market", investors usually will invest in well-known issuers' securities, only straying to smaller, more obscure issuers when sufficient information can be obtained.

72/ Some say that the recent Fiat offering failed due to deficient disclosure. See discussion in the following section.

natural market forces, 73/ national and multinational disclosure requirements, and the influence of strong disclosure systems like that of the United States contribute to the level of disclosure now found in Euromarket offerings. This mixture of influences acts to provide the current environment in which the Euromarket now operate.

4. Euroequities

a. Fast Growing Market

The mechanisms that have for many years been utilized in the initial offering and subsequent resale of Eurobonds and other debt securities are now being mobilized for the purpose of placing shares of major corporations through an international network. This new market is called the Euroequity market. 74/ The center of this market is, as is

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73/ The growing importance of the institutional investor, the highly competitive nature of the market, and the preoccupation of banks and securities dealers with maintaining their good reputations in the market have all contributed to the pressure for adequate disclosure in the market.

74/ Actually, the term "Euroequities" has been around for much longer than the phenomenon described herein. As early as 1970, it was used to describe the growing market for shares represented by International Depositary Receipts ("IDRs"), which serve much the same function in the world's markets as do American Depositary Receipts ("ADRs") in this country. See

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true in the Eurobond market, in London. Nevertheless, traditional United Kingdom share offering practices are not followed in the Euroequity market. For example, price discounts and preemptive rights, commonly associated with United Kingdom domestic deals, are usually not found in Euroequity deals. The Euroequity market is still primarily a new issue market, with most of the active secondary trading in issues taking place on the home exchange of the issuer. Despite this fact, the secondary market for Euroequities is clearly growing at a fast pace, with over 500 securities traded daily outside their home market as of May 31, 1986, as compared with only about 200 the year before. 75/ Additionally, the International Stock Exchange's Automated Quotation System ("SEAQ") quotes major international securities in a trading system modeled after the National Association of Securities Dealers' Automated Quotation System ("NASDAQ"). In fact, SEAQ quoted these international shares before "Big Bang", and before the inclusion of domestic shares in the system.

The placing of equities through traditional Euromarket syndication procedures, previously nonexistent, has become

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(. . . continued)
"Surge in Bearer Shares," Barron's, June 6, 1970, at 9-10.

75/ "Euro-equity; Euromoney for old rope," Economist, May 31, 1986, at 96 (U.S. edition at 90).

commonplace in the last few years. 76/ While only a few years ago most companies raised equity capital in one or two major markets, offerings by significant companies today typically include an international tranche. 77/ This development can be attributed to the strength of the world's equity markets in general. Equity is issued internationally for several reasons. The most commonly cited of these include the desire to obtain a broader shareholder base and to realize a price more

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76/ This is not to say that international equity offerings are new. To the contrary, international equity offerings have been conducted for decades. It is only through international placements that the largest Swiss companies, for example, can raise sufficient equity to meet their needs. This is due to the relatively small capital market in that country and the limited resources of its investors. Companies from smaller countries have traditionally gone to London or other major markets to float equity in order to keep from flooding their relatively illiquid home markets and at the same time to obtain the best prices for their shares.

77/ A single offering may be divided into two or more "tranches" which contain securities of the same class or similar classes, but which may be offered in a different manner or have slightly different terms or conditions. Offerings that are primarily based in one country and also contain an international tranche may be technically excluded from the definition of Euroequity. However, to the extent that the international tranche of these issues is distributed through an international syndicate of underwriters such as is commonly associated with the Euromarket, that portion of such an offering may be considered for the purposes of analysis as a Euroequity deal. Such deals are increasingly becoming more commonplace in large offerings. By definition, a Euroequity issue would be placed entirely through an international syndicate.

representative of international market demands for the issuer's shares. A broader offering can reach more willing investors, more efficiently reflect the worldwide demand for an equity issue, and make more difficult an unwelcome takeover bid. 78/

Another factor that will contribute to the growth of the Euroequity market is the establishment by Euroclear in April 1986 of a clearing service for international equities. Soon to be expanded, the service originally encompassed some 100 equities from five European countries. 79/

The adaptation of the traditional Eurobond placement network to the Euroequity market has not been accomplished without certain problems, however. Different approaches are being utilized but no standard method has yet gained wide acceptance. It is clear, however, that the different types of

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78/ An excellent example of this approach is that utilized by W.R. Grace in its convertible Eurobond issue early this year. The bonds are convertible into equity after five years, except in the case of a certain type of change in control, in which case investors can convert into equity at a much more attractive rate. This is thought to be the first "poison pill" brought to the Euromarket. See "The Poisoned Atmosphere for International Equities," Economist, Feb. 1, 1986, at 75.

79/ The first countries' equities to be included in the service were Belgium, West Germany, Netherlands, Sweden and Switzerland. See "Five Nation 100 Share Service Launched," Financial Times, April 21, 1986, at I-40. Despite the new service, major problems exist in international equity clearing procedures. See, e.g., "International Equity Trading," Financial Times, April 21, 1987, at III-X.

investors in debt and equity must be considered in the marketing decision-making process. Recognizing these differences, recent issues have seen two broad classifications of underwriting techniques being used by large syndicate managers.

Swiss Bank Corporation International ("SBCI") used the first of these techniques in a recent offering by Transamerica Corp. In that offering, SBCI set up separate underwriting syndicates in the countries where the securities were being offered, thus dispersing the securities geographically. This method is designed to encourage firmer placement by the regional co-managers with final investors in their respective countries. Further, the manager arguably retains a more flexible control over the flow of the issue to the marketplace, since securities can be channelled to countries where there is more demand.

Another method of syndication has been popularized by Credit Suisse First Boston ("CSFB"), and involves the use of a much smaller group of co-managers in a single underwriting syndicate. This method is based on the belief that the presence of too many co-managers adds an unnecessary management layer. With the smaller group, CSFB and others using this technique try to maintain close control over the placement of the securities, and at the same time delegate less of the management responsibilities to others at the co-management level.

Typically, the type of issuer that will come to the Euroequity market is the company with an international market for its products. This preexisting name recognition factor in foreign countries has proved very important to the placement of shares, particularly in the cases of some internationally well-known United States companies whose shares were readily accepted in the market. 80/ Other typical issuers come from countries with a limited or relatively illiquid domestic capital markets. 81/

One of the largest Euroequity deals accomplished to date (before the recent Fiat deal, discussed *infra*) was the KLM Royal Dutch Airlines flotation of 15 million shares worth the equivalent of $295 million. Recently, Electrolux rivaled the KLM offering with a nine country placement of 8 million shares worth about $276 million. These 1986 issues, when compared with numbers of the three previous years, illustrate the current rapid growth of the Euroequity market. From 1983 to 1985, all Euroequity deals completed amounted to a total of the

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80/ *See* Lohr, "Turning to Europe for Equity," New York Times, Aug. 21, 1986, at D-1, col. 3; discussion accompanying notes 63 through 65, *supra.*

81/ Examples of these companies are European multinational companies such as Nestle, Volvo, Electrolux and Daimler-Benz.

equivalent of $3.2 billion. 82/ Through August 1, 1986, Euroequity issues by ten large United States issuers 83/ have totaled over $610 million, and 37 issues around the world have raised over the equivalent of $3.1 billion. 84/ In all of 1985, there were only three issuers in this market from the United States.

b. The Fiat Offering

The recent deal involving the secondary offering of Fiat shares has temporarily given the Euroequity market a setback, at least insofar as very large issues are concerned. The $2.1 billion issue was denominated in United States dollars, 85/ and executed through a blue-chip underwriting syndicate led by Deutsche Bank Capital Markets, the London affiliate of the West German bank, and Mediobanca of Italy. Ten other top

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82/ "The Dangers of Deregulation," Financial Times, May 9, 1986, at I-21.

83/ The large corporations on this list are joined by the Student Loan Marketing Association, a quasi-government agency.

84/ "Turning to Europe for Equity," supra n.84.

85/ It may be noted that this Euroequity deal differed from most deals in that the currency denomination of the shares was different from that of the shares traded on the home listing exchange.

underwriters were included in the deal as co-lead managers, and each was assigned a geographical territory in which to place its allocated shares. The problem with the issue, which is commonly laid to overpricing of the shares as well as other factors, 86/ arose when the market price of the shares, which are quoted on the Milan Stock Exchange, fell a total of $100 million the first day after the offering was commenced.

The price of the shares was set the night the offering was commenced at about a four percent discount to the closing that day in Milan. However, that price reflected a recent run-up associated with announced bright prospects for the company, and was thus subject to significant correction. In addition to the high offering price, the underwriting syndicate had no opportunity to pre-sell the issue prior to commencement of the offering. This was due to the insistence of Libya, the selling shareholder's predecessor, on complete secrecy regarding the offering until it was formally launched. Syndicate members complained afterward of the problems they had faced in their efforts to place such huge amounts of shares instantly in the market. 87/

86/ See, e.g., "The Regulation of Euroequities," Financial Times, October 22, 1986, at I-28; "Fiat and Libya Break Up," Fortune, October 27, 1986, at 14.

87/ See "Syndicate in Fiat Sale Faces Loss," New York Times, September 30, 1986, at D-1, col. 6.

Also cited in explaining the huge losses incurred by the syndicate members 88/ was the concern of investors with the impact of such a large flotation on the share price, which is quoted only on the relatively illiquid Milan exchange. Additionally, syndicate members complained of the lack of coordination of selling efforts, with many institutional investors being called by several underwriters and thus being able to play one against another for a better price. Finally, another factor that contributed to the problem was the perceived lack of a secondary market for the shares other than that in Milan. Since the offering, however, some underwriters, including Deutsche Bank itself, have made a market in the shares in an effort to facilitate their placement. 89/

c. Some Open Issues

The tone of doom in many of the descriptions of the Fiat deal and its problems indicates that some question seriously

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88/ Early estimates ranged from $100-200 million.

89/ The lead managers complained of the lack of patience of the underwriters, saying that the syndicate should not have expected to place such a large offering in only two days. The managers blamed at least part of the downward pressure on the stock's price on underwriters who they said were unloading shares in Milan due to their failure to quickly place their allotments.

the future of the Euroequity market. 90/ The doubt apparently centers on whether these offerings of international equities can be made through traditional Eurobond syndicates accustomed to dealing in debt issues. While many dealers make a market in Eurobonds, there is a far less well-defined secondary market for equity securities, with the home market being by far the most important. The Fiat offering illustrates the lack of a true international secondary market for some equity securities, and the problems that arise when the home market is unable to absorb the impact of such a huge offering. When the home market is the only viable secondary market for a large multinational issue, the securities may tend to flow back to that market soon after they are floated, depressing the share price.

Closer analysis of some of the factors involved in the failure of the Fiat deal, however, reveals that not only the sheer size of the offering but the probability that it was overpriced contributed greatly to its demise. Others maintain that the main cause of the failure was a lack of adequate disclosure of information regarding the company. 91/ In either case, relevant inquiries will be whether the market will self-

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90/ See notes 91 and 92, supra.

91/ See "The Regulation of Euroequities," supra, n.90.

correct and whether future issues will avoid such problems in both disclosure and marketing procedures.

Another question involves the type of investor involved in the Euroequity market. According to the issuers, among their goals in undertaking an international offering is the wide, relatively permanent placement of shares among individuals. This has certain benefits which justify some of the costs associated with an international placement. It appears highly questionable, however, whether the purchasers actually targeted in the equity offerings are individuals, or are the institutional investors that are targeted in debt offerings. This is apparent in part from the Fiat deal, where institutional investors played a major role in the events causing the placement difficulties. They initially balked at the high price, then played underwriters one against another when they were approached by more than one seller. This implies that instead of a firm placement with investors who may hold the securities, most of the Euroequity deals are being placed with institutions. This market may evolve into one no different than the Eurobond market, in which for many years the predominant investor was the "Belgian dentist", 92/ but which now is becoming dominated by large institutional investors.

92/ The term is commonly used to describe the stereotypical non-sophisticated investor in the Eurobond market who has a significant amount of disposable income.

5. United States Regulatory Considerations

a. Tax Law Considerations

As noted earlier, bonds must generally be available in bearer form in order to be saleable in the Euromarket. The provisions of the Tax Equity and Fiscal Reform Act of 1982 ("TEFRA") 93/ and the Interest and Dividend Tax Compliance Act of 1983 ("IDTCA"), 94/ however, require generally that all "registration-required obligations" be issued in registered form. 95/ Due to concern from the investment banking community, which was effectively communicated to Congress during its deliberations on TEFRA, there was included in that

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93/ Pub. L. No. 97-248, 96 Stat. 324.

94/ Pub. L. No. 98-67, 97 Stat. 369. IDTCA repealed the domestic withholding tax imposed by TEFRA, but imposed further information reporting requirements and set up penalty provisions, including a 20 percent backup withholding tax, for noncompliance.

95/ Registration-required obligations are generally those offered to the public by an entity other than a natural person and having a maturity of more than one year. I.R.C. Section 163(f)(2)(A).

act an exception from the registration requirement for Eurobonds. 96/

The "Eurobond exception" requires that all bearer bonds be issued under "arrangements reasonably designed" to ensure that they are not sold (or resold in connection with the original issuance) to United States persons; that interest be payable only outside the United States; and that there be placed on the bonds, as well as on each coupon, a legend describing the restrictions thereon. 97/ Compliance with the first of these requirements necessitates generally that either an opinion of counsel be obtained to the effect that registration under the 1933 Act is not required due to distribution only to foreigners, or that there be compliance with certification and confirmation requirements in offerings registered under the 1933 Act. 98/ These conditions must be met in order to avoid

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96/ I.R.C. Section 163(f)(2)(B). See discussion in Newburg, "United States Companies and International Financings," 20 Int'l Law. 765 (1986) (hereinafter cited as "Newburg"), at 766.

97/ I.R.C. Section 163(f)(2)(B).

98/ The tax law thus incorporates applicable securities law by this indirect reference to Release 33-4708, mentioned in the next section. The Treasury regulations are more direct in incorporating the securities laws. See Treas. Reg. Section 1.163-5(c)(2)(i), T.D. 8110, 51 F.R. 45453 (1986). See also Kau, "Recent Tax Law Developments on Eurobond Financings," in Practising Law Institute, International Financial Offerings (1985), at 157-58. The second alternative may also be satisfied if the (continued . . .)

imposition of sanctions on the issuance of long-term debt in bearer form and the imposition of the 30 percent withholding tax on payments of interest to foreigners. 99/

Although the passage of the Tax Reform Act of 1984 ("TRA 1984") 100/ made it possible for United States corporations to issue bearer bonds in the Eurobond market directly instead of through an off-shore finance subsidiary, there remained the problem of information and reporting requirements imposed by TEFRA. These requirements were strengthened with the enactment in 1983 of IDTCA, which added backup withholding provisions. 101/ Under temporary Treasury regulations, however, if the issuer of the bonds has no actual knowledge that the person to whom interest payments are made is a United States person, then the information reporting and backup

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(. . . continued)
securities are exempt under either Section 3 or 4 of the 1933 Act, or if the instruments are not securities within the meaning of that Act. Treas. Reg. Section 1.163-5(c)(2).

99/ I.R.C. Section 871(a) imposes the tax on interest and original issue discount income received from sources "within the U.S." by nonresident alien individuals.

100/ Deficit Reduction Act of 1984, Pub. L. No. 98-369, 98 Stat. 494.

101/ Section 104 of IDTCA added I.R.C. Section 3406, which requires the imposition of a 20 percent backup withholding tax in the case of certain failures in the reporting system.

withholding requirements do not apply. 102/ Additionally, simultaneous offerings of bonds to United States and foreign investors may be exempt from these requirements if, for example, the offering is registered with the Commission and includes domestic and foreign tranches, the latter of which is accomplished in compliance with Commission requirements as to final placement with foreign investors.

Therefore, under the present tax laws, 103/ United States corporate issuers can offer bonds directly in the Euromarket in bearer form, so long as they are placed with foreign investors. Although a large segment of the market, the FRNs, continue to be purchased and held mostly by institutional investors who are not as concerned with the anonymity that is generally sought by individual investors in the Eurobond market, ease of resale in the secondary market still dictates that most of these issues be made in bearer form.

The United States government and both official and quasi-governmental agencies are prohibited from issuing debt obligations in bearer form under the Treasury regulations. 104/

102/ Temp. Treas. Reg. Section 1.6049-5(b)(2).

103/ The provisions of the Tax Reform Act of 1986 do not change the provisions discussed herein.

104/ Treas. Reg. Section 1.163-5(c)(1). This is despite the fact that the Code allows such issuance. *See* T.D. 7965, 49 F.R. 33228 (1984).

This restriction is also extended to issues by corporate entities that are secured more than 50 percent by such obligations. 105/ Nevertheless, such issues may be done in such a manner as to accomplish their placement "anonymously" in foreign markets. Such an offering is known as a foreign "targeted" offering or a targeted registered offering. The foreign beneficial owner of such a security need not identify itself if the registered owner is a financial institution, interest is paid to the institution outside the United States, the issuer has no actual knowledge that a United States person is the beneficial owner of the obligation, and certain elaborate certification procedures are followed. 106/ This type of procedure has been used by governmental entities, and also by corporations in connection with such issues as mortgage-backed securities (collateralized by governmental agency securities) offered abroad in bearer form.

105/ See Sept. 7, 1984 letter from Treasury Secretary Regan to Senate Finance Committee Chairman Robert Dole.

106/ I.R.C. Sections 871(h) and 881(c). See Temp. Treas. Reg. Section 35a.9999-5; Newburg, supra n.93, at 771-71.

b. Securities Laws

In 1963, in an effort to reduce the United States balance of payments deficit and defend United States gold reserves, 107/ President Kennedy created the Task Force on Promoting Increased Foreign Investment in United States Corporate Securities and Increased Foreign Financing for United States Corporations Operating Abroad, which was chaired by Henry H. Fowler (the "Fowler Task Force"). The task force was charged with developing programs in several areas: an effort by the United States financial community to market securities of United States private companies to foreign investors, and to increase the availability of foreign financing for United States business operating abroad; a review of activities that adversely affect foreign purchases of the securities of United States private companies; and identification and appraisal of restrictions of other countries that hamper efforts by United States companies to sell securities and raise capital abroad from non-United States sources. 108/

107/ The United States remained on a fixed exchange rate system with the dollar backed by and convertible into gold until 1973.

108/ "Report to the President of the United States from the Task Force on Promoting Increased Foreign Investment in United States Corporate Securities and Increased Foreign Financing for United States Corporations Operating Abroad," Henry H. Fowler, Chairman, April 27, 1964, at v.

In connection with its analysis of possible actions of the United States financial community that should be taken in order to address the perceived problems facing the nation, the Fowler Task Force was primarily concerned with, inter alia, selling United States corporate securities abroad, adapting United States corporate securities to foreign securities markets, selling United States investment company shares abroad, and attracting foreign bank deposits. 109/ As a result of its study, the Fowler Task Force made several recommendations, including that the Commission issue a release setting forth the circumstances under which it would normally issue a "no-action" letter providing that no registration be required on public offerings of securities outside of the United States to foreign purchasers, including dealers. 110/ The Commission responded on July 9, 1964 to this recommendation by adopting Securities Act Release 33-4708 ("Release 4708").

Briefly stated, Release 4708 sets forth the Commission's position that it will generally not take enforcement action regarding sales of securities without registration under the 1933 Act so long as the offering has been completed under circumstances reasonably designed to prevent the distribution or redistribution of the securities into the United States or

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109/ Id., at 5.

110/ Recommendation No.4. Id., at 7.

to United States persons living abroad. Thus, despite the use of the jurisdictional means described in the 1933 Act, 111/ the Commission has decided not to apply the registration provisions of the Act in certain outlined transactions.

The recognized procedure for assuring that securities "come to rest" abroad has been to include affirmative clauses in the underwriting and selling group agreements not to sell the securities within the United States or to United States persons, and inclusion in the confirmations of sale representations that the final investors are not United States persons, and sales restrictions are imposed in the form of a "lock-up" period during which securities may not be sold to United States investors. 112/

111/ *I.e.,* means of interstate commerce or the mails. Securities Act Section 5.

112/ The policies and practices that have developed over the years under Release 4708 are currently the subject of reconsideration by the Commission. *See* discussion in Part VI of this chapter.

III. OVERVIEW OF UNITED STATES DISTRIBUTION METHODS AND DISCLOSURE REQUIREMENTS

This section summarizes the distribution techniques and disclosure practices of the United States. The discussion emphasizes the application of these standards to foreign entities seeking to sell securities in the United States. The discussion will provide a basis to compare the disclosure and distribution standards of the countries described in Part IV.

A. JURISDICTION

The registration requirements of the Securities Act apply, unless an exemption is available, whenever a person, directly or indirectly, "make[s] use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell such security through the use or medium of any prospectus or otherwise, or carr[ies] or cause[s] to be carried through the mails or in interstate commerce, by any means or instruments of transportation, any such security for the purpose of sale or for delivery after sale." 1/ The term interstate commerce includes "trade or commerce in securities or any transportation or communication relating thereto . . . between any foreign country and any State, Territory, or the District of Columbia . . ." 2/ Pursuant to Securities Act

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1/ Securities Act Section 5(a).

2/ Securities Act Section 2(7).

Release No. 4708, however, the Commission has taken the position that registration will not be required if securities are "distributed abroad to foreign nationals even though use of jurisdictional means may be involved in the offering . . . [assuming] the distribution is to be effected in a manner which will result in the securities coming to rest abroad." 3/

The antifraud provision of the securities laws may apply, whether or not an exemption from registration is available. In connection with cases instituted under certain of the antifraud provisions the courts have applied two tests derived from international law to determine whether the federal securities laws have extraterritorial application: The conduct test and the effects test. 4/ The "conduct" test may be applied to determine whether jurisdiction over a transaction consummated at least partially abroad is appropriate due to conduct that occurred in the United States. Relevant inquiries include where the conduct in question occurred, and whether the conduct

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3/ The theory underlying this release is being reexamined in light of the changing global securities markets. See Part V, infra.

4/ See generally Schoenbaum v. Firstbrook, 405 F.2d 200 (2d Cir. 1968), modified on other grounds, 405 F.2d 215 (2d Cir. 1968) (en banc), cert. denied, 395 U.S. 906 (1969); Leasco Data Processing Equipment Corp. v. Maxwell, 468 F.2d 1326 (2d Cir. 1972); Bersch v. Drexel Firestone, Inc., 519 F.2d 974 (2d Cir. 1974), cert. denied, 423 U.S. 1018 (1975); IIT v. Cornfeld, 619 F.2d 909 (2d Cir. 1980). For an extended discussion of jurisdiction, see Chapter VII, infra.

occurring within the United States was substantial in regard to completion of the overall scheme or fraud.

The "effects" test can support jurisdiction if acts were taken abroad that caused substantial and foreseeable harm to interests within the United States. 5/ The test rests on the theory that Congress wants to protect United States investors from improper foreign transactions that have such adverse effects on United States markets as artificially influenced prices and trading volume, and the erosion of public confidence. 6/

B. UNITED STATES DISTRIBUTION TECHNIQUES

Securities which are distributed within the United States are required to be registered under the Securities Act pursuant to Section 5 of that Act unless they are otherwise exempted by the Act. Under the Securities Act, only negotiations and agreements between the issuer and underwriters, or among underwriters who will be in privity of contract with the issuer, are permitted before filing of the registration statement with the Commission.

5/ *See* Part V for an expanded discussion of the jurisdictional tests in connection with the discussion of tender offer regulation.

6/ *Id.*, at 1108.

In the typical distribution, prior to filing the registration statement an underwriting group will be created by an "agreement among underwriters." Pursuant to this agreement, representatives of the underwriters negotiate with the issuer regarding the terms of the offering. The final underwriting agreement with the issuer is generally not executed until immediately prior to effectiveness. The underwriting arrangement may be a "firm commitment," whereby the underwriters assume the market risks, or a "best efforts" agreement under which the issuer assumes the market risks.

In the agreement among underwriters, the underwriters often authorize their representatives to reserve part of the issue for selling group dealers and institutional investors. The organization of this selling group must be delayed until after the registration statement is filed.

After filing, offers (but not sales) may be freely made pursuant to a preliminary, or "red herring," prospectus. It is during this period that solicitations are made and the selling group is formed, although no sales may be made prior to the effectiveness of the registration statement.

C. DISCLOSURE REQUIREMENTS FOR PRIMARY OFFERINGS

Disclosure requirements for public offerings of securities registered under the Securities Act and for periodic reporting under the Securities Exchange Act for foreign non-governmental issuers are, in principle, the same as the requirements for domestic issuers. However, in practice, the Commission has attempted to adjust its disclosure requirements to accommodate foreign issuers. Separate registration and reporting forms have been adopted.

The registration statements available for foreign private issuers making distributions in United States markets are Forms F-1, F-2, F-3, F-4 and F-6. 7/ Form F-1 is used for initial public offerings. Forms F-2 and F-3 are available for foreign issuers that have previously registered securities under the Securities Act or the Securities Exchange Act. Forms F-2 and F-3 permit incorporation by reference of reports filed under the Securities Exchange Act, but Form F-2 requires delivery of those reports with the prospectus. Form F-3 is available only for issuers who have been reporting under the Securities Exchange Act for at least 36 months and who are "world class" issuers or are offering investment grade securities, securities issued upon exercise of certain rights or warrants, securities issued pursuant to a dividend reinvestment plan or upon

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7/ A Canadian foreign private issuer may use these forms only if it does not have or has not had during the twelve months prior to the filing of the form any class of securities registered under Section 12(b) of the Securities Exchange Act or a reporting obligation (suspended or active) under Section 15(d) of the Exchange Act and if such issuer has not issued its securities in a transaction to acquire by merger, consolidation, exchange of securities or acquisition of assets another issuer that filed or was required to file an annual report on Form 10-K.

conversion of outstanding securities or securities issued in a secondary offering. Form F-4 is available for business combinations.

Form F-6 is used for registration of American depositary shares evidenced by American depositary receipts. American depositary shares are shares issued by foreign issuers for sale in American markets. Such shares represent beneficial ownership in the foreign securities and are issued to avoid problems inherent in the ownership of foreign securities, such as collection of dividends and transfer problems. As the American depositary share is a security separate from the underlying shares of the foreign issuer, it must be registered for sale in the United States.

The disclosure required of foreign private issuers is similar to that required by domestic issuers. The principal differences are as follows:

(1) Foreign issuer financial statements must have an informational content substantially similar to that required of domestic companies. They need not be prepared in accordance with United States generally accepted accounting principles; however, they must be presented in accordance with accounting principles generally accepted in the domicile country and a reconciliation of significant variations from United States GAAP and Regulation S-X must be furnished. Reconciliation only of the differences in the measurement items (income statement and balance sheet amounts) is required in annual reports of

foreign private issuers and for offerings of certain non-convertible investment grade debt, securities issued upon exercise of certain rights, or warrants, pursuant to a dividend reinvestment plan, or upon conversion of outstanding securities. Full reconciliation of financial statements to United States generally accepted accounting principles and Regulation S-X (which sets forth the Commission's financial statement regulations) is required for other offerings.

(2) Unless a full reconciliation to United States GAAP is specified or required because of the nature of the offering or the securities, only revenue information need be broken into categories of activity and geographic markets ("segments") unless the total operating profit from each segment materially differs from their respective contributions to total sales and revenue, in which case narrative disclosure is required.

(3) Compensation of directors and officers need be disclosed only in the aggregate unless the issuer discloses such information to its shareholders or otherwise makes this information public.

(4) Information regarding transactions with management is required, but need be presented only to the extent the registrant discloses such information to its shareholders or otherwise makes public the information.

D. CONTINUOUS DISCLOSURE

Periodic reports must be filed with the Commission by any foreign private issuer with securities listed on a national securities exchange or NASDAQ (non-Canadian foreign private issuers with securities quoted on NASDAQ prior to October, 1983 are exempt from this requirement), and by issuers that have made a registered public offering in the United States. The reporting obligation for securities not listed on an Exchange or traded on NASDAQ may be suspended (except for a fiscal year in which a registration statement under the Securities Act becomes effective or is required to be updated) if the class of securities is held by less than 300 United States residents or less than 500 United States residents where the total assets of the issuer have not exceeded $5,000,000 on the last day of each of the issuer's three most recent fiscal years. 8/

The reports required are a Form 20-F, which must be filed within 6 months following the end of the issuer's fiscal year, and periodic Forms 6-K, which must be filed to furnish whatever information the issuer (1) is required to make public in the country of its domicile, in which it is incorporated, or organized pursuant to the law of that country, (2) has filed with a foreign stock exchange on which its securities are traded and which was made public by that exchange, or (3) has

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8/ 17 C.F.R. Section 240.12h-3.

distributed to its security holders. The Form 20-F calls for specific disclosure about the issuer's business, including financial statements reconciled to U.S. generally accepted accounting principles. As is the case with Securities Act filings, foreign issuer financial statements must have an informational content substantially similar to that required of domestic companies. However, they need not be prepared in accordance with U.S. generally accepted accounting principles and the Commission's Regulation S-X, if they are presented in accordance with accounting principles generally accepted in the domicile country and a reconciliation of the difference in measurement items (the income statement and balance sheet amounts) is provided.

Other foreign issuers would be required to register under the Securities Exchange Act if they have engaged in interstate commerce or in a business affecting interstate commerce or their securities are traded by use of the mails or any means or instrumentality of interstate commerce and they have assets of more than $5,000,000 and more than 500 shareholders worldwide. Exemptions from filing periodic reports are available, however, if the subject class of securities is held by fewer than 300 United States residents or the issuer furnishes to the Commission materials required to be made public pursuant to the law of the country of its domicile, required to be filed with a stock exchange on which its securities are traded and which were made public by the exchange, or materials it is required to distribute to its security holders. 9/

E. LIABILITY

This section outlines the liability provisions contained in the Securities Act. Pursuant to Section 11 of the Securities Act, any person who acquired a registered security may bring suit if any part of the registration statement, when that part became effective, contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading. The plaintiff may sue every person who signed the registration statement (including the issuer, its principal executive officer or officers, its principal financial officer, its comptroller or principal accounting officer and the majority of its board of directors or persons performing similar functions, and for a foreign issuer, its duly authorized representative in the United States); the issuer's directors, partners or persons about to become directors or partners of the issuer, "experts" who have with their consent been named within the registration statement as having prepared or certified part of the registration statement or a report or valuation used in connection with the registration statement,

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9/ 17 C.F.R. Section 240.12g3-2.

with respect to that statement, and every underwriter. Such persons are jointly and severally liable.

Reliance on the registration statement need not be proved in a claim under Section 11 unless the purchaser bought the security after the issuer had made generally available to its security holders an earnings statement covering a period of at least one year beginning after the effective date. If required, reliance may be established without proof of the reading of the registration statement. 10/

The issuer's liability is absolute unless it can show the plaintiff knew of the untruth or omission at the time of the acquisition of the security. Other defendants will not be liable if they can establish certain reasonable care defenses. 11/

Pursuant to Section 12 of the Securities Act, liability also attaches to any person who offers or sells a security in violation of Section 5, or who offers or sells a security by the use of interstate commerce or the mails by means of a prospectus or oral communication which includes misleading statements or omissions of material information. A reasonable care defense is available if the suit is based on untrue statements or omissions.

10/ Securities Act, Section 11.

11/ Securities Act, Section 11.

An action under either Section 11 or Section 12(2) must be brought within one year after the discovery of the untrue statements or the omission, or after discovery should have been made by the exercise of reasonable diligence. A suit under Section 12(1) must be brought within one year after the violation on which it is based. Further, the suits under Sections 11 and 12(1) must be brought within three years after the Security was bona fide offered to the public, and suits under Section 12(2) must be brought within three years after the sale. 12/

Section 17(a) of the Securities Act makes it unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by use of the mails, directly or indirectly (1) to employ any device, scheme or artifice to defraud; (2) to obtain money or property by means of any untrue statement or omission; or (3) to engage in any transaction, practice or course of business which operates or would operate as a fraud or deceit upon the purchaser. This section is applicable to any offer or sale, not just those involved in registered offerings. Similarly, Securities Exchange Act Section 10(b) and Rule 10b-5 make it unlawful to engage in this conduct in connection with the purchase or sale of any security.

12/ Securities Act, Section 13.

IV. FOREIGN DISTRIBUTION METHODS, DISCLOSURE SYSTEMS AND LIABILITY PROVISIONS

The following discussion outlines the disclosure requirements and distribution practices for securities issued and sold in the European Economic Community ("EEC") and eight major industrialized nations other than the United States. The discussion of the EEC centers around several EEC Council directives that have been issued in connection with the program of harmonization of companies laws of the member states, and which focus on disclosure requirements for securities that are to be listed on exchanges and accounting practices within the Community.

Each of the eight countries is then individually addressed according to the same format. The discussions focus on the various regulatory structures found in the countries and the nature of their implementing authorities. Major securities markets are identified and the means by which securities are commonly distributed therein are outlined. Liability provisions in the various countries are mentioned in each section. Currency translations are provided as appropriate in historic terms or at current exchange rates (December 1986).

A. EUROPEAN ECONOMIC COMMUNITY

Several of the countries discussed in subsequent parts of this chapter are members of the European Economic Community (the "EEC"). Member states of the EEC have agreed, pursuant to the Treaty of Rome, to adopt and implement directives issued by the EEC Council of Ministers (the "Council"). The Council has adopted several directives proposed by the Commission of the EEC dealing generally with the harmonization of certain aspects of corporate and securities laws of the member states, including some disclosure provisions, and is considering the adoption of others.

The adoption of the various directives is in keeping with one of the goals of the EEC, which is to promote the abolition of obstacles to the free flow of capital among member states. The work being done in the area of securities regulation and stock exchange listing requirements is intended to smooth the operation of the EEC's stock exchanges and promote greater interpenetration of those markets. 1/

The procedure by which a Council directive becomes the law of a member state is complex and lengthy. 2/ The EEC

1/ G. Imbert, "Experience at the European Community Level," paper presented at the XI Annual Conference of the International Association of Securities Commissions (July 16, 1986).

2/ Directives differ from regulations in several respects, including the method of their implementation. While regulations are self-implementing and become law within the various member states without any further action by them, directives merely instruct the member states to pass laws that will implement the spirit of the directive. The period within which a particular directive must be implemented is uniform among the member states, but may vary for different individual directives.

Commission is responsible for drafting and recommending directives for issuance by the Council. Once a draft directive has been completed by the Commission, it is then studied by the Council and its staff. The input of member states is received at each stage of the process.

After the Council issues a directive, it must be adopted and implemented by the member states individually; however, each member state retains the right to choose the form or method of implementation. Absent a disagreement between the Commission and a member state, implementation is effected when a member state submits to the Commission a copy of legislation which, in the member state's opinion, fulfills its obligations under the directives. The terms of a given directive will establish a time period within which this must occur. Thus, the fact that a directive has been issued by the Council does not mean that it is the law of all member states. To the contrary, many of the directives mentioned below have not been fully implemented by several of the member states. Failure to implement a directive by a member state may subject it to infringement proceedings before the Commission.

The directives relevant to this study include those regarding admission of securities to listing on an exchange; disclosure by companies which have listed securities or which propose to sell to the public securities that are to be listed; and minimal accounting standards.

1. Directives Regarding Securities to be Listed on an Exchange

The Council of the EEC has adopted three directives regarding listing requirements in an effort to, among other things, provide equivalent protection to investors at the Community level, facilitate the listing of companies on the various exchanges of the member states, and achieve greater interpenetration of national securities markets within the Community in order to contribute to the establishment of a European capital market.

Official action by the member states to implement the directives was to be accomplished by June 30, 1983. As of April 1987, all member states, with the exception of Portugal and Belgium, had implemented the directives. Portugal has submitted draft legislation which is being modified to achieve compliance. Belgium, however, has not yet passed legislation that complies with the terms of the directives.

a. Listing Directive

The first of the directives regarding listing requirements is the Council Directive of 5 March 1979 coordinating the conditions for the admission of securities to official stock exchange listing (the "Listing Directive"). 3/ In addition to giving details of minimum conditions that must be met prior to listing on an exchange in a member state, the Listing Directive sets forth certain continuing obligations of issuers whose securities are so listed. 4/ The terms of the Listing Directive clearly indicate that member states have discretion to require such further information as is necessary to protect investors or to ensure the smooth operation of the market. 5/ Broad, simultaneous dissemination is to be made of the information required on a continuing basis. 6/

The conditions for listing are not extensive. 7/ In the case of shares of common stock, the company and the shares to be listed must be in compliance with the laws to which the company is subject. The company must have a minimum

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3/ 22 O.J. Eur. Comm. (No. L 66) 22 (1979). The directive need not be applied to certain unit trusts and investment companies or to securities issued by governmental entities of the member states. Art. 1.

4/ The specified conditions may in certain cases be made more stringent regarding both listing and continuing obligations. Listing Directive, Arts. 5.1, 5.2.

5/ Listing Directive, Art. 13.

6/ Listing Directive, Art. 17.

7/ These are set forth in the Listing Directive at Schedule A for the admission of shares and Schedule B for the admission of debt securities to listing.

capitalization of at least one million European Currency Units ("ECU"), 8/ and must have published or filed at the appropriate domestic agency its annual reports for the three financial years preceding the application for admission to listing. The shares must be freely negotiable and widely enough distributed to the public to ensure proper operation of the market for the shares. 9/

Similar requirements concerning legality of the securities and the company's status must be met with regard to debt obligations. The minimum amount of the subject debt offering must be at least 200,000 ECU, except in certain cases where a deviation is appropriate and a sufficient market for the debt securities will exist. Exchangeable or convertible debt

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8/ The Directive actually refers to "European units of account". However, by Council Regulation of Dec. 20, 1980, 23 O.J. Eur. Comm. (No. L 345) 1 (1980), promulgated after the adoption of the ECU, all references in official EEC documents, including the Listing Directive, to European units of account were replaced by the ECU. ECU's are artificially created currency units comprised of a "basket" of currencies of several of the member states. Thus, the particular value at any given time of an ECU vis-a-vis another European currency that is included in the basket will vary according to applicable foreign exchange rates. Notably absent from the basket of currencies comprising the ECU is the British pound sterling.

9/ This requirement is deemed to be satisfied when at least 25 percent of the subject class of shares is distributed to the public, but may be satisfied with a lower percentage if there is a large number of shares outstanding.

instruments and those to which a warrant is attached may be listed only if the underlying securities are listed on a recognized exchange.

The Listing Directive sets forth certain continuing obligations for issuers of shares and debt obligations listed on an exchange. 10/ Such issuers must, among other things, (1) ensure equal treatment for all security holders in the same position; (2) ensure, at least in each member state where its securities are listed, that all necessary facilities and information are available to enable security holders to exercise their rights; (3) make available to the public, as soon as possible, its most recent annual accounts and annual report; (4) inform the public as soon as possible about any major new developments in its sphere of activity which are not public knowledge and which may lead to substantial movements in the prices of its shares or may significantly affect its ability to meet its obligations; and (5) if the issuer has securities listed on more than one exchange, assure that the same information is made available to the market of each of those exchanges.

10/ Listing Directive, Schedules C and D, respectively.

b. Information Directive

Disclosure of information regarding securities being offered to the public that are to be listed on an exchange is the subject of a separate directive. Standards for disclosure are set forth in the Council Directive of 17 March 1980 coordinating the requirements for the drawing up, scrutiny and distribution of the listing particulars to be published for the admission of securities to official stock exchange listing (the "Information Directive"). 11/

Admission of securities to listing on an exchange must be conditioned upon the publication of an information sheet regarding the issuer and the securities to be listed. 12/ The information required is that which is necessary "to enable investors and their investment advisers to make an informed assessment of the assets and liabilities, financial position, profits and losses, and prospects of the issuer and of the rights attaching" to the subject securities. 13/ Thus, in addition to required disclosures in the Schedules to the Information Directive, the Directive calls for that information

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11/ 23 O.J. Eur. Comm. (No. L 100) 1 (1980).

12/ Information Directive, Art. 3.

13/ Information Directive, Art. 4.

which is necessary to meet the foregoing standard. 14/ Provision for exemption from the obligation to publish information may be made by the member states in certain enumerated cases. 15/

The scope of the required information depends on the nature of the security being offered and the persons to whom it is offered. 16/ The information is to be supplemented by the annual accounts for the latest financial year of the issuer. The areas of required disclosure for shares (and other equity related offerings) generally cover information concerning (1)

14/ Information Directive, Art. 5.1.

15/ For example, publication may not be required upon application for listing for securities that have been the subject of a public issue, that were issued in connection with a takeover offer or in connection with certain merger transactions if, within the past 12 months, a document containing information substantially equivalent to that required by the Information Directive has been published. Other exemptions may be instituted by the member states for, among others, securities allotted free of charge to existing security holders, or shares issued pursuant to conversion or rights.

16/ Distinctions are made between shares and convertible or exchangeable securities offered on a preemptive basis, those offered to the public in general, debt securities of an issuer that already has securities listed on the same stock exchange, debt securities that because of their nature are bought and traded largely by a limited number of investors who are knowledgeable in investment matters, securities issued by financial institutions or guaranteed by a separate entity, and convertible or exchangeable debt securities. Information Directive, Arts. 8 through 17.

those responsible for preparing the document and for auditing of accounts; (2) the shares and the listing application; (3) the issuer and its capital; (4) the activities of the issuer; (5) the assets and liabilities, financial position and profits and losses of the issuer; (6) administration, management and supervision of the issuer; and (7) recent developments and prospects for the issuer. 17/ Areas of disclosure for debt securities include generally the same types of information, except information concerning loans of the company instead of a description of the company's shares is given. 18/ In the case of certificates representing shares, additional information must be given regarding the issuer of the certificates and regarding the certificates themselves. 19/

The Information Directive also specifies certain arrangements to be established for the scrutiny and publication of the information required. No such information may be published until the document has been approved by the competent authorities of the appropriate member state, who must determine that the document contains all information required by the

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17/ Information Directive, Schedule A.

18/ Information Directive, Schedule B.

19/ Information Directive, Schedule C.

Information Directive. 20/ The information must be published a "reasonable period" before the listing is to become effective, and should either be inserted in a widely circulated newspaper or provided in a free brochure.

Significant differences exist between the Information Directive requirements and comparable United States disclosure requirements. A few examples of disclosure requirements under the Directive illustrate these differences: (1) with respect to segment information, the Information Directive requires only a breakdown of net turnover by category of activity and geographical markets for the previous three years; (2) only the total amount of remuneration paid to administrative, management and supervisory bodies must be disclosed; (3) only comparatively limited information concerning unusual transactions between the issuer and management must be given, as must the total of all outstanding loans to administrative, management and supervisory bodies; (4) limited information regarding business experience and background of management is required; and (5) disclosure of shareholder interests below an established threshold need not be made, and this threshold may be set by member states at as high as 20 percent of the equity. In each case, the United States securities laws would require greater disclosure. It also should be noted that a number of EEC disclosure requirements of the Information Directive are

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20/ Information Directive, Art. 18.

applicable only in the case of equity related offerings and do not apply to debt securities. Further, the Information Directive applies only to securities which are to be listed on an exchange. 21/

c. Interim Report Directive

The third directive regarding requirements for issuers with securities listed on an exchange is the Council Directive of 15 February 1982 on information to be published on a regular basis by companies with shares that have been admitted to official stock-exchange listing (the "Interim Report Directive"). 22/ The Interim Report Directive applies only to equity related securities. 23/ The Interim Report Directive

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21/ This difference would be eliminated should the proposed directive for disclosure by companies whose securities are not to be listed on an exchange be adopted by the Council and implemented by the member states. The proposed directive was submitted by the Commission to the Council on Jan. 13, 1981, and a revised text was submitted on July 19, 1982, but no formal Council action has yet been taken.

22/ 25 O.J. Eur. Comm. (No. L 48) 26 (1982).

23/ The Interim Report Directive actually applies only to issuers who have shares listed on an exchange. However, because the Listing Directive requires that underlying shares be listed for all listed convertible or exchangeable debentures or those with warrants attached, issuers of such debt securities are also covered by its terms.

requires generally that issuers publish half-yearly reports on their activities and profits and losses during the first six months of each financial year. 24/ It must be published within four months of the end of the period, and must include figures as well as explanatory notes. 25/ The report is to be published in a widely circulated newspaper or otherwise made easily available to the public, and must also be sent to the competent authorities in the appropriate member state. 26/

2. Accounting Directives

The EEC, as a part of its general effort to harmonize the laws relating to companies, has also issued three directives relating to accounting standards. The Fourth Council Directive of 25 July 1978 regulates the contents of the annual accounts and reports of issuers that must be disseminated in accordance with the requirements of other directives. 27/ The directive includes minimum standards for balance sheets and profit and loss accounts, establishes valuation rules and prescribes rules

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24/ Interim Report Directive, Art. 2.

25/ Interim Report Directive, Art. 4.

26/ Interim Report Directive, Arts. 7, 8.

27/ 21 O.J. Eur. Comm. (No. L 222) 11 (1978).

for the content of annual reports and notes to the annual accounts. It also requires auditing of the annual accounts.

The Seventh Council Directive of 13 June 1983 provides for drawing up of consolidated accounts and annual reports for parent enterprises with one or more subsidiaries. 28/ It prescribes the layout and contents of the accounts and reports and also requires that they be audited. Finally, the Eighth Council Directive of 10 April 1984 provides standards for education, training and testing of auditors and qualification of auditing firms. 29/

28/ 26 O.J. Eur. Comm. (No. L 193) 1 (1983).

29/ 27 O.J. Eur. Comm. (No. L 126) 20 (1984). For further discussion of accounting standards in various countries, *see* Chapter IV, *infra*.

B. UNITED KINGDOM

The structure and the activities of the securities market in the United Kingdom are in an extremely fluid state. This is due principally to the ending, in October 1986, of certain restrictive practices on The Stock Exchange in London (the "Stock Exchange") 1/ -- the "Big Bang" -- and the recent creation by legislation of a new regulatory system. This section therefore discusses both the regulatory system in effect at the time of writing and that which is soon to become effective, insofar as details are available.

Investor confidence in the prior self-regulated financial and securities market has been undermined in recent years by several financial scandals, and the new system, although still dependent on self-regulation, reflects an attempt to restore public and international confidence. The changes are intended to re-establish London as the world's largest and most internationalized securities market. London's geographical location makes it a natural center, together with New York and Tokyo, of the emerging 24-hour global securities market.

To a large extent, the international and domestic markets are interrelated in London. This section of the report,

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1/ The term "Stock Exchange" refers to a single organization that regulates the activities of the various stock exchanges located around the United Kingdom. The Stock Exchange has recently changed its name, pursuant to reorganization, to the International Stock Exchange of the United Kingdom and the Republic of Ireland.

however, focuses principally on the United Kingdom domestic securities markets. 2/

1. Description of Statutory Scheme and Regulatory Authority

a. Source of Regulation

There is no comprehensive body of securities law in the United Kingdom, and no single agency is responsible for administration of securities matters. Matters such as the registration of new companies with, and the grant of incorporation by, the Registrar of Companies, the contents of prospectuses and liabilities for misstatements therein, and the duties of officers and directors were, until recently, governed by the common law as supplemented by the Companies Act 1985 (the "Companies Act"). 3/ The recent Financial Services Act 1986 (the "Financial Services Act") 4/ has superseded or will

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2/ While discussion of the securities markets in this paper relates to securities activities throughout the United Kingdom (the vast majority of which takes place in London), certain aspects of the regulatory system discussed herein relate only to Great Britain and not to Northern Ireland.

3/ 1985 Chapter 6.

4/ 1986 Chapter 60.

supersede many of the Companies Act provisions relating to prospectus disclosure.

Under the Financial Services Act and the Companies Act, all prospectuses and annual reports (which must include audited accounts) are filed with the Registrar of Companies, who is responsible to the Department of Trade and Industry ("DTI"). 5/ In addition to such statutory provisions, disclosure and reporting requirements are imposed (by authority granted under the Financial Services Act) by the Stock Exchange for companies listed thereon. Additionally, both the rules of the Stock Exchange and the City Code on Takeovers and Mergers, applicable to most large companies, prescribe the disclosures to be made to shareholders in the event of a takeover bid and the manner in which such transactions shall be conducted. The Stock Exchange is an independent body and the City Code, which is not backed by force of law, is administered by the City Panel, staffed by appointees from the securities industry.

The regulatory framework regarding marketing of shares and the issue of shares on takeover or exchange was established

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5/ New regulations to be drafted pursuant to the provisions of the Financial Services Act will replace the Companies Act requirements relating to the contents of prospectuses for unlisted securities. Practitioners expect the new requirements to be closer to the disclosure requirements presently applicable to securities listed on the Stock Exchange. The requirements are expected to be published later in 1987; this paper considers the requirements presently in effect under the Companies Act.

principally by the Prevention of Frauds (Investment) Act 1958 and is now also covered by the Financial Services Act.

Regulation of securities professionals depended until recently on whether they were members of the Stock Exchange, which sets examination, capital requirements and other qualifications for membership. Under the new regulatory framework established by the Financial Services Act, all persons who "carry on investment business" in the United Kingdom must register with the Securities and Investment Board ("SIB"), an agency funded by the securities industry with powers delegated by Parliament.

b. Extent of Regulation

The scope of regulations concerning the issue and trading of securities is somewhat less extensive than in the United States. The initial raising of capital is less expensive in that less filings and the employment of fewer professional advisors are involved, and requires less disclosure than in the United States, especially for those companies which do not list on the Stock Exchange. 6/ While an offer of securities to the

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6/ See discussion of markets in the next section. Disclosure required under the Companies Act which, apart from the general legal requirement of disclosure of material facts, is all that applies at present to non-listed companies, is not extensive. See discussion of disclosure requirements. For a variety of reasons, arguably cultural, United Kingdom (continued . . .)

public (the Financial Services Act refers to an offer by "advertisement") must be made by a prospectus containing the disclosures set out in the Companies Act, a wholly private offering -- a sale of unlisted securities to institutional investors, for example -- need not even comply with these requirements, and no filings or applications for exemption need be made. 7/ Disclosure requirements for Stock Exchange listed companies are more comparable to those of the United States (see below), but prospectuses still tend to be shorter.

While the raising of capital by unlisted companies is not subject to qualitative review, issues of securities for which listing is sought are subject to the qualitative review by the Quotations Department of the Stock Exchange described below.

(. . . continued)
prospectuses are more concise, and drafted with a less stringent view on materiality, than their United States counterparts. Factors involved are generally thought to be the much lower rate of corporate litigation in the United Kingdom, the lack of class action suits and contingency fees, and the larger proportion of sophisticated institutional investors in the United Kingdom.

7/ There is very little case law on the nature of a private offering. As discussed below, the requirement to register a prospectus under the Financial Services Act is premised on the use of an "advertisement", an undefined term. There is, of course, no judicial interpretation of this term as yet.

c. Jurisdiction

The extent of extra-territorial jurisdiction claimed by the UK regulatory agencies has never been subject to much discussion. Sections 159 and 160 of the Financial Services Act (for listed and unlisted securities, respectively) provide that no advertisement offering securities on a stock exchange or to the public may be issued "in the United Kingdom" without registration of a prospectus. No attempt is made to regulate the sale of securities to United Kingdom citizens overseas, and British companies making offerings totally overseas are not required to register their prospectuses in the United Kingdom.

2. Nature of Securities Markets

The United Kingdom securities market has a considerable international flavor. As of autumn 1986, securities of companies and governmental agencies from at least 37 countries were listed on the Exchange. 8/

The Stock Exchange ranks third in the world in terms of market capitalization, with approximately £1,353 billion ($2,000 billion) as of the end of 1986. Of this, equity

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8/ The Republic of Ireland exchanges are also accommodated within the Stock Exchange. Additionally, the Stock Exchange has a computer-linked office in Johannesburg to facilitate transfer of London-listed South African securities.

represents some £284 billion ($419 billion). Some 6,840 securities are listed on the Stock Exchange, of which 4,980 are company securities, 607 are public sector securities, and 1,253 are Eurobond issues. 9/ Securities may either be fully listed on the Stock Exchange 10/ or traded through the Unlisted Securities Market ("USM"). The USM was established by the Exchange in 1980 as a forum off the floor of the Stock Exchange 11/ for small or new companies with a need for capital but an insufficient track record for full listing. Compared to the Stock Exchange's five-year requirement, USM companies need only to have been traded for three years. USM quotation costs are approximately half those of full listing. 12/ Some 360

9/ Stock Exchange Quarterly, Autumn 1986.

10/ To list on the Stock Exchange, a company must have published or filed accounts in accordance with its national law covering the five years preceding application for listing (although the Exchange has discretion to modify this requirement). The company must not have relationships with substantial shareholders that could result in conflicts of interest and the securities for which it applies for listing must have an expected market value of £700,000 (currently about $1,032,500) for equity, and £200,000 (currently about $295,000) for debt.

11/ Most trading of fully listed securities now also takes place off the Exchange floor.

12/ Such costs account for approximately 1-1/2 to 2 percent of the amount raised. This compares favorably to NASDAQ quotation upon a primary offering, for example, which usually amounts to around 5 to 7 percent of the amount raised.

companies of the 496 originally listed on the USM are still traded there and about 50 are now fully listed on the Stock Exchange. Present USM companies have capitalization of between £600,000 and £137 million (currently about $885,000 and $202 million), and have proved particularly attractive to individual shareholders. 13/

The Stock Exchange also provides, by its rule 163(2), a facility for occasional dealings in the securities of unlisted and unquoted companies through Stock Exchange brokers, who will find buyers and sellers. Before the Exchange will grant permission for such a deal to be made, evidence of "genuine business activity", the company's latest accounts and copies of any recent prospectuses must be submitted to the Department of Quotations.

The UK over-the-counter ("OTC") market is run by specialist organizations dealing in the securities of an increasing number of companies not traded on the Exchange, some of which are fairly substantial. These firms may act as market makers, as brokers matching buying and selling orders, or both. Trading is predominantly by telephone. Investors may also contact an unlisted issuing company directly, to ascertain whether the secretary knows of an interested buyer or seller. Such sales are not regulated. OTC trading of listed securities is permitted in the United Kingdom.

13/ Statistics are as of Autumn 1986.

In 1986, the Stock Exchange established an electronic "Third Market" on which the equity securities of small United Kingdom companies not meeting the listing requirements of the Exchange or the USM may be traded in lieu of trading on the OTC market. Sponsors of companies applying to list on this market must arrange for at least two market-makers to deal in these companies' shares.

3. Issuers

Domestic as well as foreign companies and governmental agencies raise money in the United Kingdom securities markets. In general, no distinction is made between residents and non-residents in the capital-raising process. Foreign issuers are led numerically by the United States, with Japanese, Canadian, German, South African and Dutch issuers following substantially behind. United States issuers represent over six percent of the total capitalization of the USM.

United Kingdom government bonds ("gilts") are issued by the Bank of England acting as agent for the government. All domestic company issuers in the capital markets are public companies, which comprise the great majority of United Kingdom companies. Private companies (those registered as such with the Registrar of Companies in order to take advantage of the greater privacy afforded thereby) are precluded from raising funds in the public markets.

As of the beginning of 1986, there were 2,688 companies with equity shares listed on the Stock Exchange. Foreign companies accounted for 572 of this total. Of the listed companies, 89 were newly authorized in 1985 to list their equity on the Stock Exchange, with 17 of these being foreign issuers. There were new listings in 1985 of bonds and debentures totalling £57 billion ($73,884.2 million), as compared with listings of £34 billion ($45,397.2 million) on the Stock Exchange in 1984. The domestic private sector accounted for £10 billion ($12,559.6 million) of the 1985 total, the domestic government for £20 billion ($26,245.8 million) and £27 billion ($35,078.7 million) were international issues. 14/

4. Types of Securities Traded

Debt, equity and convertible securities of all the issuers described above are traded in the United Kingdom securities markets. The value of domestic debt securities exceeds that of equity securities, but trading volume in equity securities is higher.

Government bonds are the most widely traded instrument in the United Kingdom and have a deep and liquid market. Such

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14/ International bonds include Eurobonds and foreign bonds.

securities account for 90 percent of the value of fixed interest securities and 80 per cent of the value of all securities issued in the United Kingdom, but only 20 percent of the volume of securities traded, since investors tend to hold them longer than other types of securities. The remaining fixed interest securities are issued by public companies. In addition to frequently taking advantage of the status of a Stock Exchange listing for Eurobonds (see Part II, supra), foreign issuers often choose to issue "Bulldog Bonds" (sterling denominated debt securities managed by British banks).

The full range of securities traded in the United Kingdom markets, debt and equity, are listed on the Stock Exchange. Both debt and equity securities may be listed on the USM, but the majority of issues are equity. Equity securities are issued in registered form, while debt securities may be issued in either registered or bearer form. Rights issues are common, although the former strict regulations requiring the issuance of preemptive rights by companies have been relaxed. Rights issues may be traded on the Stock Exchange.

Two types of options, "traditional" and "traded", are available in the United Kingdom. Traditional options may only be granted by the company, and may not be traded subsequently. Traded options are closer to United States options, in that they may be bought or sold at any time, and are available on the stocks of many United Kingdom companies. There is also a market in unit and investment trusts (mutual funds). As of late 1986, there were approximately 900 unit trusts in the United Kingdom with a value of around £21 billion ($30 billion), approximately one-tenth of the value of United States mutual funds. A market for limited partnership interests does not seem to have evolved.

5. Primary Offerings

a. Participants in a Distribution

In the primary market, corporate securities are issued and usually underwritten by a merchant bank or stockbroker (the "issuing house"), although debt securities are not always underwritten. Most important domestic issues are listed on the Stock Exchange, and an applicant for listing must appoint a member of the Stock Exchange to sponsor its application. This sponsor is responsible, among other things, for ensuring that the Quotations Department of the Stock Exchange is given all information which should be brought to its attention and for lodging with the Department all the documents required to support the application for listing.

The nature of the sponsoring institutions is presently undergoing change. As part of the run-up to the "Big Bang", foreign individuals and domestic and foreign corporations have been allowed to acquire interests in member firms of the Stock Exchange, and the composition of the participants in primary securities offerings has changed dramatically. Banks are not prohibited from securities activities and a number of banks (overseas branches of American banks in particular, because their securities activities are restricted in their home market under the Glass-Steagall Act), have acquired interests in or formed partnerships with Stock Exchange member firms.

The usual way in which shares or debentures are offered to the public is by an "offer for sale". The issuing house agrees to purchase or subscribe for a block of securities, then offers them to the public at a (higher) fixed price or by means of a "tender". 15/ The public is invited to submit applications on forms attached to the prospectus. The issuing house renounces its allotment in favor of the applicants, thereby saving stamp duty, which is payable on the transfer of securities. Although the securities are actually sold by the issuing house, for disclosure purposes the Companies Act treats the document distributed to the public as a prospectus issued by the issuer. The sponsor arranges for financial institutions, either brokers or banks, to underwrite the issue. The underwriters agree to

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15/ A tender offer invites subscribers to offer to buy shares at a price that is determined by reference to the bids submitted. Shares are distributed to the highest bidding subscribers at a uniform price which is based upon the lowest bid at which a sufficient number of equal or higher bids exists such that the number of securities bid for by such bidders equals the amount of securities to be sold in the offering.

take up shares in the event that the public does not submit sufficient applications. 16/

Alternatively, securities may be "placed" directly with financial institutions. This involves distribution without advertisement to a number of institutions and others who have already indicated interest. Since this method favors the large investor and deprives small investors of an opportunity to acquire securities at bargain prices, the Stock Exchange requires that at least 25 percent of the securities of the class being issued (10 percent for the USM) be in public hands (whether in the United Kingdom or elsewhere). Such placings require special approval by the Stock Exchange.

Placings may be made in one of two ways. An issuing house may subscribe for the issue and then invite its clients (e.g., insurance companies and pension funds) to purchase from it at a higher price. Alternatively, an issuing house or stockbrokers or a bank may, without subscribing, act as agents for the company and invite their clients to purchase securities from the company. Placings are often used for issues of foreign securities, where there is less likely to be public interest in the issue. They are the most common method of distribution on the USM.

16/ It is also possible to make a direct invitation by prospectus to the public. This method is rarely used except by government borrowers.

Typically, a large issue of securities involves a lead manager, a group of managers, and a selling group, which may also be underwriters. In order to participate in the distribution of securities in the United Kingdom, institutions must be either authorized to do so or exempt under the Financial Services Act. The lead manager usually has an agreement with the company setting out their respective roles and including certain warranties and undertakings by the company as to the accuracy of the documents being distributed. This agreement sets out the basis of remuneration for the managers and the various commissions payable either by the managers or the company to the parties involved in the distribution.

The Bank of England exercises control over the timing of issues of sterling securities where the amount of money to be raised is £3,000,000 or more, in order to maintain an orderly new issue market. The sponsor of a primary offering must apply for a date known as "impact day," upon which the size and terms of the issue may be announced. The publication requirements of the Stock Exchange ensure that investors are aware of new issues and can apply for printed prospectuses and application forms. Typically, the prospectus appears in advertisement form in at least one newspaper.

There has been a recent trend towards security ownership by individuals. 17/ This trend has been encouraged by the current British government in the recent sales of shares in nationalized industries. One aspect of new issues favoring the small investor is that all subscriptions of 500 shares or less are usually filled even if the issue is oversubscribed. Institutional purchases are cut back, if necessary, to ensure that members of the investing public get the shares they request. Nevertheless, historically, the investors in whose hands primary distributions have ended up have been largely institutions, and large institutional investors such as pension funds and insurance companies still hold half of all securities issued.

b. Disclosure and Review

In general, the nature of the disclosure to be made by an issuer depends on whether the securities are to be listed (on the Stock Exchange or the USM) or unlisted. If the decision is made to list the securities, the nature of the disclosure further depends on whether the offering is by an issuer who has been listed previously on the Stock Exchange.

The Companies Act (soon to be superseded by regulations under the Financial Services Act) regulates the contents of

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17/ Recent polls indicate that just over 8 percent of the population owns shares (MORI, June 1986).

prospectuses for securities (listed or unlisted) offered by advertisement. 18/ The Financial Services Act provides for exemptions from the prospectus requirement to be granted by the DTI's Secretary of State, inter alia, where an advertisement has a "private character" (possibly by reason of a connection between the person issuing it and those to whom the advertisement is addressed) and advertisements addressed to persons "sufficiently expert to understand any risks involved."

The current statutory textual disclosure requirements are principally set out in the Third Schedule to the Companies Act, and are designed mainly to provide information about:

- The directors and what benefit they will receive from their directorships;
- The profit being made by the promoters;
- The amount of capital required by the company to be subscribed, the amount actually received or to be received in cash, and the precise nature of the consideration given for the remaining capital;
- The company's financial history;

18/ The concept of an "advertisement" plays a similar role to the ideas of "public offerings" or "distributions" in other countries' securities laws. Only public companies may invite the public to subscribe for shares. Private companies (i.e.- all those not registered at Companies House as public companies) are subject to an effective embargo on access to the capital markets and must raise their capital privately.

- The company's obligations under contracts into which it has entered, and for commission and preliminary expenses;
- The voting and dividend rights of each class of shares; and
- The nature of assets to be acquired with the proceeds of the offering.

Financial disclosures are prescribed by the Fourth Schedule of the Companies Act and must include:

- A report by the company's auditors, dealing with the profits or losses in each of the five financial years immediately preceding the issue of the prospectus (or since incorporation) and giving the rates of dividends paid on each class of shares during the same period;
- Assets and liabilities of the company as of the last date which the accounts were made up;
- If a company has subsidiaries, profits and losses and assets and liabilities either for each subsidiary individually or for the group on a consolidated basis; and
- If the proceeds of the securities to be issued are to be applied to the purchase of a business or of shares in another company, an accountants' report

on the profits or losses of such business or company for the last five financial years, and its assets and liabilities as of the last date on which accounts were made up.

A draft directive of the EEC, which would increase somewhat the disclosure requirements relating to securities not listed on a stock exchange, will, if adopted by the Council of the European Communities, require EEC member states to prescribe prospectus requirements comparable to those for listed securities (discussed below). 19/

Compared with United States disclosure requirements, both financial and non-financial disclosures under the Third and Fourth Schedules are much less extensive. Compensation of directors is only addressed to the extent that it is governed by any provisions in the articles (which are comparable to the by-laws of a United States corporation). Neither the employment histories of the directors nor the amounts of compensation paid to them are required to be disclosed. The projected use of the capital raised need only be detailed in so far as it involves working capital or the purchase of property. The accounts required by the Schedules are also much less extensive than in the United States. Segment reporting is required for classes of business in respect of turnover and

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19/ *See* discussion in III.A., *supra.*

profit and loss, and for geographical markets in respect of turnover. This information may be withheld, however, if the directors believe it to be in the company's interests to do so.

Copies of prospectuses must be filed with the Registrar of Companies before the date of their publication. 20/ The copies must be signed by all the company's directors, and must have attached to them the consent of any expert named in the prospectus to the use of the expert's report. Copies of contracts described in the prospectus must be attached, as must a statement concerning adjustments permitted to be made in accountants' reports. Prospectuses that comply with these requirements are registered by the Registrar, after which they may be used. There is no substantive or merit review of such prospectuses.

More extensive disclosure is required in the prospectuses or "listing particulars" used for securities to be listed on the Stock Exchange. It should also be noted that listing particulars are required in some cases, such as rights issues, where the Financial Services Act deems that no advertisement is

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20/ In the case of very large issues (such as the recent British Telecom and British Gas issues) and Eurobonds it is customary to circulate a "pathfinder" prospectus amongst interested institutions to gauge interest in the issue. Such prospectuses are filed with the Registrar of Companies and in the case of large issues (although not generally with Eurobonds) with the Stock Exchange. There are no statutory provisions or Stock Exchange rules relating to pathfinder prospectuses.

made and that therefore no prospectus need be registered. The disclosure requirements established by the Council of the Stock Exchange are set out in "Admission to Securities for Listing," known as the "Yellow Book," and include and expand upon disclosure requirements established by the EEC for all exchange-traded securities. These requirements are incorporated in most EEC member-countries' statute books.

Disclosure of information regarding the issuer of listed securities is in general comparable to that required by the United States in Regulation S-K and Form 20-F. The disclosure covers:

- Identification of the company, the persons responsible for statements made in the prospectus, and the issuer's auditors, bankers, brokers, and lawyers;
- The securities issued, including exchanges where listed;
- Nature and amount of issue, and details of other securities outstanding;
- Rights of the securities being issued and how they may be affected by the rights of other securities;
- Price, method of distribution and method of delivery of securities;
- Estimated net proceeds and commissions paid;
- Details of the issuer's capitalization;
- Identification of controlling persons;

- Description of the issuer's activities, including a breakdown of net turnover in the last 3 years by categories of activity and by geographical markets, if material (segment information);
- Description of management, including names, addresses and functions of directors and founders (if a new business), other business interests of such persons, details of service contracts, aggregate remuneration paid to directors and estimate of amounts to be paid during the current year;
- Recent trends in the issuer's business and its prospect for the current financial (fiscal) year; and
- Where forecasts are made, the assumptions forming the basis for such forecasts.

Financial disclosure under the Yellow Book includes:

- Independent accountants' reports covering profits and losses, assets and liabilities, financial record and position of the issuer (and its group, if applicable) for each of the last 5 financial years;
- Where such financials are more than 9 months old, interim financials covering the first six months of the current financial year;
- A statement that the annual accounts are audited (or if not, why not) and an indication of other

information in the listing particulars that has been audited by the auditors;

- Profit or loss per share of the issuer for the last 3 financial years and the amount of dividend per share for such years;
- Any significant changes in the financial or trading position of the issuer or group since the date of the latest financials;
- A table showing the source and application of funds of the issuer (or group) over each of the past 3 financial years;
- Details of holdings in companies representing 10 percent or more of the issuer's capital and reserves or its net profit or loss;
- Consolidation principles used; and
- Disclosure as of the most recent practicable date (on a consolidated basis if material) of the issuer's loan capital outstanding, total amount of other indebtedness, mortgages and charges and contingent liabilities.

The Stock Exchange requires accounts of companies incorporated outside the United Kingdom to be prepared in conformity with international accounting standards as promulgated by the International Accounting Standards Committee and specified by the Exchange. At present compliance with the

International Accounting Standard relating to segment reporting is not required.

Principal differences between the requirements of the Stock Exchange and the United States focus on the disclosures required regarding director remuneration, the age of financial statements and the extent to which segment information is required. Prospectuses in the United Kingdom tend to be more forward looking generally than those used in the United States.

USM disclosure requirements generally cover the same matters as those covered by the Yellow Book, but in more general terms and with less specific disclosure required. In particular, less detailed information is required regarding the terms of the issue and the nature of the securities offered. Financial disclosure is somewhat less detailed than in the case of listed companies, and there is no requirement that financials be audited. Financials must be produced for the latest five financial years, or since incorporation. Material changes, if any, since the date of the last accounts, must be described. The prospectus must contain a statement to the effect that the securities described will not be admitted to full listing on the Stock Exchange.

Upon application for listing with the Stock Exchange, the applicant company is required to file substantial documentation with the Quotations Department for review. This documentation includes:

- An application form signed by the sponsor and supported by two member firms prepared to register as dealers of the security;
- Copies of the Listing Particulars, one of which is signed and dated by each director;
- Information on the company and its directors;
- The company's constitutional documents and board resolutions relating to the offering;
- Specimen certificates representing the securities; and
- Other documentation supporting the issue, including a letter from the sponsor regarding the accuracy of the director's opinion as to the adequacy of working capital.

Copies of these documents generally are submitted some four weeks prior to hearing of the application by a panel of the Quotations Committee. Final proofs are submitted 14 days prior to the hearing; the actual documents two days before the hearing. Prior to this formal meeting, the staff of the Quotations Department will have reviewed the documentation. The panel's decision on admission is given at the hearing. The Stock Exchange is authorized by regulation to reject an application to listing if, in its opinion, the company's situation is such that admission would be detrimental to investors' interests. In exercising this qualitative judgment, the Stock Exchange relies to a certain extent on the sponsor's heavy responsibility under the Exchange's rules to ensure that a company is suitable for listing on the Exchange and that its directors are prepared to comply with the Exchange's reporting requirements.

By regulation there is a right to judicial review of the Stock Exchange's decision. Judicial review is limited to consideration of whether such a decision is within the Exchange's authority and has been arrived at on reasonable grounds by fair procedures.

Upon acceptance for listing, listing particulars may be distributed. The Stock Exchange requires publication of listing particulars and notices of the issue in newspapers. Where listing particulars are published in a newspaper, the address at which printed copies of the listing particulars are available must be stated.

No material distinctions are drawn between new and established issuers, and the Stock Exchange disclosure provisions outlined above apply equally to an issue of securities by an issuer that has made offerings previously. Listing particulars are not required, however, where the shares to be issued are of a class already listed, and either the issue will not increase that class by more than ten percent, or the shares issued will be allotted to employees. When an issuer whose shares are already listed issues shares by way of rights, less disclosure is required, although listing particulars are still required. Debt offerings by issuers who have any type of securities already listed, or convertible debt offerings by issuers whose shares are already listed, require somewhat less disclosure, although more than would be required under a fully integrated disclosure system.

6. Secondary Market

Most multi-capacity securities dealers, particularly retail banks and stockbrokers, are involved in secondary trading. Merchant (investment) banks usually limit their secondary trading to large blocks of securities. Many individual stockholders are involved in the secondary market, although large institutional investors are the major participants in the secondary government securities market.

Continuing reporting obligations are imposed by both the Companies Act and the Stock Exchange. 21/ The Companies Act requires that annual returns be filed with the Registrar of Companies. These set out the company's registered office, the location of its share and debenture registers, capitalization,

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21/ As in primary trading, prospectuses are not required unless offers are made to the public. The Financial Services Act provides that registered prospectuses must be used in "secondary offers". These include offers made by advertisement by persons who acquired securities from the issuer with the intention of issuing such an advertisement, where the securities are not listed and have not been held as an investment by the offeror, or where the offeror is a controlling person of the issuer.

calls on shares, details of indebtedness, lists of past and present members, and its directors and secretary. The Companies Act also requires that annual financial reports be sent to shareholders at least 21 days before the shareholders meeting at which such reports are to be approved. However, accounts need not be filed with the Registrar. The shareholders meeting of public companies must take place within seven months of the end of the fiscal year.

The Stock Exchange's continuing disclosure requirements, many of which arise from EEC directives, cover the following:

- Annual reports and accounts, to be issued within six months of the end of the relevant financial period;
- Half-yearly or interim reports which need not be audited, to be sent to holders of securities or published in newspapers; and
- Directors' reports to accompany annual accounts, explaining why results differ from any forecasts, providing a geographical analysis of turnover and net contribution, and detailing the company's borrowing, the country of operation of subsidiaries, the amount of interest capitalized, any material contracts, and the directors' interests in shares. If applicable, the report must also state that shareholders have no pre-emptive rights as to new shares.

Generally, listed companies have a duty to disclose information necessary to prevent a false market arising in their securities, and the Stock Exchange prescribes regulations regarding the activities of listed companies to this end.

7. Liability

Under the Financial Services Act, the persons "responsible" for listing particulars or prospectuses are liable to pay compensation to persons suffering loss by reason of untrue or misleading statements therein. Reasonable belief in the accuracy of a statement or the propriety of an omission is a defense. "Persons responsible" include the issuer, its directors, and persons named as accepting responsibility for the document or authorizing the contents of any part of it. Actions under the common law torts of negligent misstatement and deceit may also be available to aggrieved investors.

The Financial Services Act also imposes criminal liability for breach of its requirements relating to prospectus disclosure.

8. Rating System, Withholding Tax, Limitations on Transferability

The United Kingdom has no rating agencies similar to those operating in the United States. However, a new credit rating agency, EuroRatings Ltd., issued its first ratings on March 9, 1987, from its London office. Promoted and majority-owned by Fitch Investors Service, Inc. of New York, EuroRatings has been designed with the stated goal of providing a full service rating system for the international markets. Although the agency will rate Sterling issues, it will concentrate on all types of issues in the Euromarket, including Eurocommercial paper and Eurobonds offered by both private and sovereign issuers, and will also rate international bonds.

Withholding taxes are payable on interest earnings except where reduced or eliminated by tax treaties, and while dividends are declared net of advance corporation tax ("ACT"), residents of countries that have tax treaties with the UK may claim a tax credit for the amount of ACT paid, less a withholding tax of 15 percent.

Stamp duty of half of one percent is payable on the transfer of securities, whether in the primary or secondary markets. This has been reduced in recent years from two percent.

Under English law, there is no restriction on transfer of securities to foreigners. No distinction is made between resident and non-resident investors. There are no currency exchange controls, so the proceeds of investments may be repatriated easily.

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C. JAPAN

1. Description of Statutory Scheme and Regulatory Authority

The basic body of Japanese securities law is contained in its Securities and Exchange Law of 1948 (the "SEL") which is patterned on the United States Securities Act and Securities Exchange Act. 1/ The principal aspects of the SEL are: (1) registration and disclosure requirements applicable to primary offerings; (2) periodic disclosure requirements; (3) proxy, insider trading and short-swing profit provisions; (4) provisions regulating securities companies and exchanges; (5) civil and criminal liability provisions; and (6) a prohibition against commercial banks engaging in securities business. 2/ The Japanese

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1/ Law No. 25, April 13, 1948.

2/ Act 65 of the SEL prohibits banks, trust corporations, and certain other financial institutions from engaging in any securities business except where (1) the bank purchases or sells securities on written order from, and for account of, a client; (2) the transaction is made for its own investment purposes and/or for the account of its trustors' accounts on the basis of trust contracts pursuant to the provisions of other laws; or (3) the transaction involves government or municipal bonds, corporate bonds or debentures and other debt securities with respect to which principal and interest are guaranteed by the government. The SEL provisions are currently under attack by the banking industry in much the same way as is the Glass-Steagall Act in the United States.

Japanese securities laws are administered by the Securities Bureau of the Ministry of Finance ("MOF"). Cabinet and MOF orders and rules of self-regulatory organizations 3/ supplement Japanese securities legislation. In particular, numerous regulations have been promulgated interpreting the SEL and forms have been adopted setting forth required disclosure for various types of offerings. The principal regulations regarding public offerings of securities are:

(1) Securities and Exchange Law Enforcement Order (Cabinet Order No. 321);

(2) Ministerial Ordinance Concerning Registration, etc. of Public Offerings or Secondary Distributions of Securities (MOF Ordinance No. 5); and

(3) Ministerial Ordinance Concerning Registration, etc., with Respect to Public Offering or Secondary Distribution of Foreign Government Bonds, etc. (MOF Ordinance No. 26).

2. Nature of Securities Markets

There are eight stock exchanges in Japan: Tokyo, Osaka, Nagoya, Kyoto, Hiroshima, Fukuoka, Niigata and Sapporo. The

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3/ The Securities Dealers Association of Japan and the stock exchanges are the primary self-regulatory organizations.

Tokyo, Osaka and Nagoya exchanges each have, in addition to the regular market, a "second section" for the listing of equity shares in which the number of listed shares, shareholders or volume of trading is relatively small compared with the regular trading market. 4/ Foreign securities may be listed only on the "foreign section" of the Tokyo Stock Exchange (the "TSE").

Each securities exchange has regulations governing the purchase and sale of securities and the listing and delisting of securities. The SEL prohibits any person other than a registered securities exchange from establishing any facility that is similar to an exchange. Commission rates are generally set by each exchange.

Stock exchange rules generally require exchange members to trade listed securities, whether debt or equity, only on the exchanges. There are exceptions, however, such as one permitting block trades of bonds, which results in a large portion of debt trading taking place off the exchanges. Virtually all trading of listed stocks is done on the exchanges.

An issuer of securities traded over-the-counter must register the securities with the Securities Dealers Association as over-the-counter securities. The number of securities registered in this manner is small, apparently because of the

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4/ Listing requirements for the second sections are less strict than those on the principal exchange.

second sections of the exchanges. The association has registration standards that are similar to the listing standards of the securities exchanges.

The market had a capitalization of Y277.8 trillion ($1,746 billion) at the end of 1986 based on domestic exchange-listed stocks with market value of investment companies excluded. From 1984 to 1986, the Japanese equity market grew 68 percent (measured in United States dollars).

3. Issuers

The number of domestic companies listed on the TSE at the beginning of 1986 was 1,499. The number of companies traded on the Tokyo Stock Exchange foreign section reached 55 as of March 1987, up from 21 at the end of 1985. 5/

4. Types of Securities Traded

Japan's bond market has expanded rapidly during the past decade, with government bonds the most widely traded of the debt securities. Total trading volume of bonds on the TSE and the over-the-counter markets in Tokyo increased to Y2,826 trillion ($16.7 trillion) in 1986, from Y2,288 trillion ($9.6

5/ United States companies account for 33 of these. See Chapter 2, Table 14.

trillion) in 1985. There were 854 listed debt issues on the TSE at the beginning of 1986.

In addition to yen-denominated bonds issued by Japanese residents, a large market exists for bonds issued by foreign persons or in foreign currencies in Japan. Among the various types of foreign bonds are "samurai" bonds (yen denominated bonds), "shogun" bonds (bonds denominated in a foreign currency, usually dollars), and "sushi" bonds (similar to shogun bonds, but issued by a Japanese company).

5. Primary Offerings

a. Participants in a Distribution

Underwriting syndicates composed of Japanese securities firms handle the bulk of debt and equity issues in Japan, which may be made on a firm commitment or a best efforts basis. Japanese commercial banks are prohibited from engaging in the distribution of securities. Foreign securities firms are prohibited from participating in securities transactions with any person residing in Japan unless they have obtained a license from the MOF or the transaction is made through a licensed firm.

b. Disclosure Requirements

The SEL prohibits any public offering or secondary distribution of securities 6/ unless a registration statement is in effect with respect to such offering. 7/ Under the SEL, similar to the United States statutory scheme, certain transactions and securities are specifically exempted from operation of the Act. The term "public offering" is defined as "a solicitation of an offer to acquire securities which are to be newly issued from unspecified, many persons on uniform terms." 8/ The term "secondary distribution" means "an offer

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6/ Unlike the United States securities laws, the SEL does not include investment contracts in its definition of security. Thus, interests in Japanese limited liability companies, limited partnerships, voting trust certificates and securities depositary certificates are not considered to be securities. Certificates in securities investment trusts and loan trusts are exempt from registration under the SEL but are regulated by the Securities Investment Trust Law and the Loan Trust Law.

7/ The entire registration statement is to be made available for public inspection at the Ministry of Finance, the exchange on which securities of the issuer are listed (or the securities dealers association with which securities of the issuer are registered) and the principal or main branch offices of the issuer.

8/ SEL, Art. 2, Section 3. The MOF has taken the position that the registration requirements also extend to rights offerings, which constitute the principal method of raising funds by registered issuers. The incidence of capital formation by rights offerings is a matter of custom, since

(continued . . .)

to sell or a solicitation of an offer to buy securities which are issued and outstanding to or from unspecified, many persons on uniform terms." 9/ Ministry of Finance guidelines provide that an offering to more than about 50 is an offer to "many".

Public offerings or secondary distributions with an aggregate issue or selling price of less than Y100 million (currently about $624,000) are generally exempt (this aggregate amount includes any exempted public offering of the issuer within the past two years). 10/ The registration and prospectus delivery requirements do not apply to Japanese government bonds, to certain secured bonds or to certain other securities issued pursuant to special statutes.

Once a registration statement is filed, an offer to sell or the solicitation of an offer to buy may be made but securities may not be sold until the registration statement is effective. 11/ The registration statement technically becomes effective 30 days after filing. The current practice, however, is for the registration statement to be declared effective on

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(. . . continued)
Japanese corporate laws do not impose preemptive rights.

9/ SEL, Art. 2, Section 4.

10/ SEL, Art. 4; MOF Ordinance No. 5, Art. 2.

11/ A shelf registration system is scheduled to be introduced next year.

the second full business day following the final amendment to the registration statement. A prospectus must be delivered by the seller (or the underwriter or securities company) before or simultaneous with the sale. These prospectus delivery requirements apply for a period of three months from the date of filing (except for securities listed on a securities exchange) with respect to sales of the remaining part of securities unacquired after the public offering.

The registration statement must include audited, but unconsolidated, financial statements for the latest two fiscal years. Balance sheets and profit and loss statements for an additional 3 years must be filed with the registration statement, but need not be included in the prospectus.

Disclosure requirements are prescribed by forms published by the MOF under its rulemaking authority, as further supplemented by interpretive rules and releases. The Japanese disclosure system requires substantially less disclosure than that required by the Securities Act of 1933. For example, Japan does not have legal requirements for registrants to include any additional material information necessary to make the required statements not misleading. At present, there is uncertainty as to whether the registrant's obligations are satisfied merely by the mechanical process of responding to specific items in the registration form.

Textual disclosure requirements include:

- Detailed description of the securities offered and the terms thereof, legal rights thereunder and corporate authority;
- Use of proceeds;
- Issuer information (generally limited to a brief history, schedule-type reconciliation of the issuer's capital stock, shareholder schedules, ratio and statistical data, and market data);
- Schedules listing subsidiaries, officers and directors and employees;
- Outlines of the business including business objectives, nature of the company's business and material management contracts;
- Description of the business operations and facilities focusing on manufacturing capacity, orders received and sales results;
- Description of the issuer's financial condition for and at the end of the last two fiscal years, including the contents of principal asset, liability and income and expense accounts; and
- A cash flow projection for the six month period immediately following the most recent recorded period with accompanying production goals, expansion plans and an explanation of difficulties foreseen in their accomplishment.

Japan's textual requirements thus do not include many significant 1933 Act disclosure concepts such as summaries of the offering, risk factors, transactions with management, executive compensation, management's discussion and analysis, and dilution. However, for diversified corporations, the registration statement must describe the business carried out by the registrant and the major products and the relative weights of each line of business. Issuers also must state the amount of production, orders and sales of each product for two fiscal years, including the monthly average. Profit and loss information as to lines of business, such as separate net income, is not currently required. However, the MOF has decided that companies with listed stocks will be obligated beginning in spring of 1988 to disclose the divisional or regional profit and loss, or segment information. The MOF is currently undertaking a study of the contents and method of disclosure of segment information, taking into consideration concerns of investors and industry.

There has been a recent simplification of the disclosure system applicable to registration statements for companies which have disclosed information continuously for at least five years. For such companies, the annual report will be allowed to be incorporated by reference in the registration statement, and effectiveness of the registration statement may be declared as early as 15 days after filing.

With a few exceptions, the distribution practices and disclosure requirements for non-Japanese issuers are similar to those of Japanese issuers. Generally, foreign issuers are required to have pre-filing conferences with the Corporate Finance and Capital Market Divisions of the MOF's Securities Bureau and also with the International Finance Bureau. Foreign issuers are also required to obtain a certification under the Foreign Exchange and Trade Control Law of 1949 prior to issuance. Registration documents must be submitted in English and Japanese and a Japanese agent must be appointed.

If the MOF determines, on an individual basis, that it is not detrimental to Japanese investors and the public interest, financial statements may be prepared in accordance with the GAAP of a foreign issuer's domicile and certified by auditors in the issuer's domicile in accordance with its domestic GAAS. If the financial statements published in the home country are consolidated, only those need be included. The registration form for foreign issuers requires prospectus disclosure of the differences from Japanese accounting principles together with disclosure of legislation and tax laws in the issuer's domicile affecting Japanese investors. Supplemental Japanese audits are not required.

c. Listing Requirements

To be listed, a company must file an application with the exchange. The application will be examined by the exchange in accordance with the exchange's listing regulations. If, after conducting its examination, the exchange considers listing appropriate, it will authorize listing subject to the approval of the MOF. A foreign company seeking listing must appoint a securities company from among members of the exchange to process the application. Generally, an application for listing is slightly more detailed than an annual securities report filed under the SEL and includes unconsolidated financial statements for the last three years and consolidated financial statements for the last two years.

The listing criteria for foreign applicants on the TSE differ from those for domestic companies in that slightly higher standards are required in certain areas. Generally, to avoid restrictions on the number of shares that may be traded, at least 20 million shares of a foreign company must be listed. "Good liquidity" must exist in the home market, and shareholders' equity must exceed Y10 billion (currently about $62.4 million), or Y1 billion (currently about $6.2 million) for domestic companies. Net profit before taxes must have exceeded Y2 billion (currently about $1.2 million) for the last three business years (for domestic companies this requirement is Y400 million (currently about $2.5 million), Y300 million (currently about $1.9 million) and Y200 million (currently about $1.2 million), respectively, for the last three business years). There is no restriction on the transfer of shares once listed.

The TSE has no rules regarding the voting rights of shareholders. As a matter of policy, however, it does not permit listing of ordinary stocks with no voting rights, in order to promote responsiveness of corporate management. Nevertheless, in special cases the Exchange has permitted shares with limited voting rights to be listed. 12/ Preferred stocks may be issued without voting rights, so long as the right to vote is given if a dividend payment is not made. 13/

6. Secondary Market

a. Purchasers

Equity ownership at the beginning of 1986 was distributed as follows: financial institutions, 39.6 percent; individuals, 26.3 percent; business corporations, 25.9 percent; foreigners, 6.1 percent; securities companies and government, 2.1 percent.

12/ As of March 12, 1987, three stocks with limited voting rights, all of them Swedish, were listed on the TSE.

13/ Commercial Code, Art. 242, para. 1. As of March 12, 1987, only one preferred stock was listed on the TSE.

The principal purchasers of debt are banks and other institutional investors.

Foreign investment in Japanese equity securities has increased substantially. Foreign purchases of stocks increased dramatically in 1980, when the Foreign Exchange and Foreign Trade Control Law of 1980 14/ ("FEL") eased investment procedures for foreign investors and lifted ceilings on foreign investment in a specific company. This trend lasted through 1983, but in 1984, 1985 and 1986 there was a net disinvestment by foreign persons in Japanese stocks. Foreign investment in Japanese bonds also declined in 1986, with net purchases totalling $2.3 billion (Y386 billion) in 1986.

b. Continuous Disclosure Obligations

Issuers of (a) securities listed on any Japanese securities exchange, (b) securities registered with a securities dealers' association as over-the-counter quoted securities, and (c) securities that are not listed or quoted but are subject to a registration requirement under the SEL (that have not obtained an exemption from the MOF) are required to file with the MOF annual, semi-annual and extraordinary

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14/ Law No. 228, Dec.1, 1949.

reports. 15/ The Exchange requires foreign companies to file quarterly reports as well. The financial statements contained in the annual report need not be consolidated; however, consolidated financial statements for the last two fiscal years must be attached. The semi-annual report must be filed within three months after the end of the first half of the fiscal year by domestic companies and within six months by foreign companies. The semi-annual report must contain audited financial statements.

Extraordinary reports must be filed promptly upon the occurrence of certain events. These include:

(1) the issuance of securities abroad;
(2) the issuance of securities in excess of Y100 million (currently about $624,000);
(3) changes in parent corporations or subsidiaries;
(4) changes in the identity of major stockholders; and
(5) material adverse events.

The Japanese Commercial Code also requires preparation of annual financial statements. These financial statements are slightly different from those prepared under the SEL. Accordingly, most public Japanese corporations prepare at least two sets of financial statements. The exchanges also impose

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15/ SEL, Art. 24.

requirements for submission of reports and for notification and disclosure of material information.

7. Liability

The liability provisions of the SEL were originally modeled after Sections 11, 12 and 13 of the Securities Act, although they have been amended, first to narrow their scope, then to strengthen the system of civil liability. 16/

Civil liabilities are imposed under the SEL as follows: (1) on the issuer, persons who make a secondary distribution, underwriters and securities companies for violation of the prohibition on sale of unregistered securities or failure to deliver a prospectus in a public offering or secondary distribution requiring registration; 17/ (2) on any person "who had another person acquire securities by use of a prospectus" or representation containing misstatements or omissions of material facts; 18/ (3) on the issuer, officers, persons who make a secondary distribution, certified public accountants and underwriters for misstatements or omissions in

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16/ The SEL also contains criminal provisions.

17/ SEL, Arts. 15 and 16.

18/ SEL, Art. 17.

the registration statement; 19/ (4) on officers and the owner in a secondary distribution for misstatements or omissions in the prospectus to any person who "acquired the securities in response to the public offering or secondary distribution and being delivered the prospectus in connection therewith." 20/ Liability is also imposed for violations of prohibitions on market manipulation, short-swing trading and similar provisions.

Defenses are available where the person who acquired the securities knew of any untruth or omission. In the case of misleading statements or omissions in the registration statement or prospectus, due diligence defenses are provided to persons other than the issuer.

8. Transfer Taxes, Rating System, Foreign Exchange Control

Securities transfer taxes are payable by a seller depending on whether the seller is a securities company. The tax on sale of shares is 0.18 percent for a securities company and 0.55 percent for other persons. For privately issued bonds, the tax is 0.015 percent for securities companies and 0.045 percent for others. For government bonds, the tax is

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19/ SEL, Arts. 18, 19, and 21.

20/ SEL, Art. 21.

0.01 percent for securities companies and 0.03 percent for other persons.

At present, there are four rating agencies in Japan. These credit agencies are the Japan Bond Research Institute, Japan Credit Rating Agency, Ltd., Mikuni & Co. and the Nippon Investors Service, Inc. 21/ The latter two rate only domestic corporate bonds, while the Japan Credit Rating Agency rates only domestic commercial paper. The Japan Bond Research Institute rates not only commercial paper and corporate bonds but international bonds issued by both private companies and sovereign states as well. These ratings are used in determining compliance with certain eligibility standards for samurai bonds and for Euroyen bonds issued by non-residents.

The FEL subjects certain transactions to prior notification and/or clearance of varying degrees by the MOF. The standards for approval have apparently been relaxed over the last few years. Pursuant to the FEL, notification is required for (1) issues of securities outside Japan by Japanese residents; (2) issues of foreign currency securities within Japan by Japanese residents; (3) issues of securities within Japan by Japanese non-residents; (4) flotation outside Japan of yen-denominated securities; (5) acquisitions of more than a certain percentage of foreign securities by a Japanese

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21/ Mikuni & Co. is the only one of these rating agencies not formally recognized by the Ministry of Finance.

resident; and (6) secondary acquisitions whereby a resident of Japan buys foreign currency securities from a non-resident, or a non-resident acquires securities (regardless of currency) from a resident unless a regulated securities company participates in or is party to the transaction.

The acquisition of common shares by a non-resident of Japan from a Japanese resident (whether an individual or a corporation) from or through a MOF-designated Japanese securities company acting as intermediary is in general not subject to any restriction. However, if the result of such acquisition is that a particular foreign investor will hold ten percent or more of the total common shares outstanding of a Japanese company, the non-resident must file a report prior to the acquisition with the MOF. Similarly, acquisitions by non-residents of shares from other non-residents are unrestricted unless the ten percent threshold is reached.

D. CANADA

1. Description of Statutory Scheme and Regulatory Authority

Canada has a federal system of government, with legislative authority over particular subject matters allocated between the federal and provincial levels of government. Securities regulation, like most aspects of corporate law, is under provincial jurisdiction. Federal jurisdiction exists over certain federally-incorporated corporations, banks, and financial institutions. Transactions in the securities of such entities may therefore be subject to federal as well as provincial regulation.

Each of the ten Canadian provinces and two territories has its own securities legislation, although the laws of British Columbia, Alberta, Manitoba, Saskatchewan and Ontario are very similar. 1/ Compliance with the requirements of any one of these provinces will normally ensure acceptability in the others. The provincial securities commissions are headed by administrators appointed by the various provincial and territorial governments.

1/ Ontario's securities legislation, introduced in 1945, was the first modern Canadian legislation on this topic, and emphasizes full disclosure. Its Securities Act of 1966, upon which the other four provinces' acts are patterned, is referred to as the Uniform Act.

While in theory the provincial authorities are of equal power, the Ontario Securities Commission ("OSC") and, more recently, the Commission des valeurs mobilieres du Quebec (Quebec Securities Commission or "QSC") and the Alberta Securities Commission have wielded greater influence than the others. This discussion will therefore concentrate on the requirements of these authorities, especially those of the OSC.

Subject to certain exemptions outlined below, all primary distributions of securities are prohibited unless the trader of securities is registered, and the securities are "qualified for sale" -- that is, registered by the filing of a prospectus or similar document with the relevant commission.

Prospectus disclosure requirements are derived from the respective provinces' securities acts, regulations, and forms prescribed under such regulations and apply whether or not the securities to be issued are to be listed on a stock exchange. 2/ In general, no additional or alternative disclosure is required by any of the Canadian stock exchanges. 3/

2/ Some provinces' company law statutes also include provisions regulating the issuance of securities, but in general defer to the securities acts in matters such as disclosure.

3/ The Toronto Stock Exchange ("TSE") and the OSC have, however, recently developed the Exchange Offering Prospectus. This is designed to foster capital formation by junior mining and industrial companies. By complying with rules prescribed by the TSE, an (continued . . .)

Additionally, various Policy Statements supplement or interpret securities legislation and regulations. Because each province has a different (although often very similar) securities act, Canadian securities administrators meet semi-annually to coordinate requirements, and their association publishes National Policy Statements. Uniform Act Policy Statements are published by the five Uniform Act provinces, and most provinces have their own Policy Statements issued by their securities commissions.

The provinces' securities acts cover such matters as insider trading and liability for misstatements in prospectuses. Securities fraud and most other matters concerning regulation of the securities markets are dealt with at a federal level under the provisions of the Criminal Code of Canada.

Securities professionals are regulated by the provincial securities commissions. No person may trade in securities or act as underwriter unless registered with the appropriate securities commission or exempt from registration.

In Ontario, for example, securities dealers are divided into several categories. The principal categories include brokers, who are registered to trade securities as principals

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(. . . continued)
issuer may raise up to C$5,000,000 (currently about US$3.6 million) by distributing its shares through the TSE without having to comply with the OSC's prospectus requirements.

or agents and who are members of the Toronto Stock Exchange ("TSE"); investment dealers; securities dealers (who may trade as principal or agent but who are not members of the TSE); and mutual fund dealers. Other jurisdictions have similar categories. Persons registered as brokers or dealers in Ontario are deemed to have been registered as underwriters. In some jurisdictions, self-regulatory organizations have been delegated full or partial authority to approve registration of their member firms' officers and sales staff. Provincial securities administrators are also charged with the recognition and regulation of stock exchanges in their provinces.

Regulation of the Canadian securities markets resembles that of the United States in both nature and scope, except for the localized nature of the regulation. The jurisdiction of the Canadian provinces is not necessarily asserted in securities transactions not taking place in or affecting the province in question, although the statutory provisions are broad enough on their face to enable such an exercise. For example, the broad definitions found in the Ontario Securities Act imply that a distribution of securities outside Ontario by either Ontario or non-Ontario issuers might, given certain jurisdictional links, require compliance with the prospectus registration provisions of Ontario law. An interpretation note published by the OSC concludes, however, that where reasonable steps are taken to ensure that an offering of securities comes to rest outside Ontario, a prospectus complying with the

Securities Act or an exemption from the provisions thereof will not be required. Extraterritorial offerings are therefore viewed in much the same way as in the United States under Securities Act Release No. 4708.

An issuer making a distribution of securities from Quebec to persons outside Quebec must, under Section 12 of Quebec's Securities Act, prepare and register a prospectus unless the QSC grants an exemption (or does not object to the offering upon receipt of certain information.) 4/ Such application for an exemption has been refused only once to date.

2. Nature of the Securities Markets

The principal Canadian capital markets are in Ontario. The Toronto Stock Exchange ("TSE") is one of the world's largest exchanges in terms of both capitalization and trading volume. Other exchanges are located in Montreal, Vancouver, Calgary and Winnipeg, but the TSE accounts for 75 percent of the total value of stocks traded in Canada.

Montreal accounted for over 20 percent of the total volume of shares in Canada until 1977, when the provincial legislature

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4/ Under Quebec Securities Act Regulations Section 115, this information includes the date of the distribution, estimate of the value of securities, the authority that will be reviewing the offering documents, a copy of the documents filed with that authority, and the name of the dealer to be used.

established French as the official language of Quebec. Banks and other financial institutions relocated to Toronto and by 1980 trading volume in Montreal had fallen by half. Volume has risen somewhat since then.

The Vancouver Stock Exchange ("VSE") styles itself a venture capital market for the natural resources industry. It has less stringent listing requirements than other Canadian exchanges and accepts listings from many speculative mining and energy resource companies. Shares are somewhat comparable to United States penny stocks and trading volume is very high.

The Alberta Stock Exchange in Calgary lists mostly regional securities and junior resource companies. The Winnipeg Stock Exchange has no trading floor, and trading, mostly in oil, mining and energy related stocks, is conducted by telephone.

An active over-the-counter market, the only market in which debt securities may be purchased, is maintained between investment dealers and brokers. Transactions may also be made through a chartered bank.

3. Issuers

Canada's bond market is dominated by the government. Both the federal and provincial governments issue securities. Corporate issuers issue both debt and equity securities, but many Canadian companies are owned by United States corporations which raise capital on a group-wide basis in the United States. There are therefore fewer corporate issuers in the Canadian capital markets than the size of the Canadian economy would lead one to expect. Foreign issuers seldom raise capital in the Canadian markets.

As of the beginning of 1986, there were 966 companies with equity shares listed on the TSE. Foreign companies accounted for only 54 of this total. Of the listed companies, 73 were newly authorized in 1985 to list their equity on the TSE, with 4 of those being foreign issuers. On the Montreal exchange as of the beginning of 1986 there were 490 companies with equity shares listed. Foreign companies accounted for only 19 of this total. Of the listed companies, 71 were newly authorized in 1985 to list their equity on the Montreal exchange, with one of those being a foreign issuer.

4. Types of Securities Traded

A wide variety of instruments, comparable to those available in the United States, are issued and traded in the Canadian markets. Most of these are traded on the stock exchanges, although debt securities, both government and corporate, are confined to the over-the-counter market and are not listed on any exchange. Both registered and bearer form bonds are available and interest is typically paid semi-annually.

Options are available on many stocks. The Montreal Stock Exchange used to account for half of the volume of options trading, but this has now dropped to around one quarter. In recent years, the VSE has introduced silver and Canadian currency options.

Mutual funds are growing in size and popularity. Shares in mutual funds are not listed and may be purchased from fund managers.

5. Primary Offerings

a. Participants in a Distribution

Securities firms may act as underwriters of, and best efforts agents for, public offerings of securities. 5/ Banks have previously been restricted in their securities activities, although at least one bank has entered the market recently by confining its participation to one province, thereby avoiding federal regulation. Recent changes in federal regulations allow banks to participate at the inter-provincial level through ownership of securities dealers. It is likely that participants in the future will include several foreign (mostly United States, United Kingdom and Japanese) firms as

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5/ Best efforts offerings are relatively rare in Canada.

limitations on foreign participation in the securities markets are lifted.

In a large deal, one investment dealer typically will act as a lead underwriter and be responsible for forming a co-underwriting group or syndicate. Formal documentation will govern the relationship and liabilities between the underwriter and the issuer and among the co-underwriters or syndicate group members.

Advertisements for public offerings are limited to "tombstones," and may be made once the relevant securities commission issues a receipt for a final prospectus.

The parties to whom a public offering will be sold will depend on factors such as the type of security, the nature of the issuer and the size of the issue. Securities firms, banks, investment companies and trust companies all are significant purchasers of new issues, and substantial portions of new issues typically are sold to institutions. Many financial institutions face strict regulation regarding the type of investments they can make; thus legal opinions on the suitability of the securities for purchase by such institutions are often included in the prospectus.

As of late 1986, approximately 9 percent of the Canadian population owned securities individually. This figure is lower than the percentage in the United States but higher than most other developed countries.

Typically, when a corporation offers shares to the public, its shares are first traded in the over-the-counter market until the listing requirements of one of the Canadian stock exchanges are met (the Exchange Offering Prospectus procedure is an exception to this.) Private placements account for a significant portion of all the securities issues made in Canada.

b. Disclosure and Review

As stated above, primary distributions of securities to the public 6/ are prohibited unless the securities are "qualified for sale" by a prospectus or similar document. Exemptions from prospectus disclosure requirements are provided for certain transactions as specified by the provincial legislatures. In Ontario, such transactions include sales of securities to banks and certain financial institutions, sales to "exempt" (e.g., sophisticated) purchasers, issues of securities in exchange for assets, limited offerings, issues of

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6/ Ontario applies its requirements to all "distributions" whether to the public or not. "Distribution" means trades in previously unissued securities, trades in previously issued securities that have been repurchased by the issuer, trades in control blocks of securities and certain trades by underwriters. Quebec, which also applies its requirements to "distributions", deems attempts to obtain subscribers for securities to be distributions.

securities in certain mergers and reorganizations, certain transactions with employees or underwriters, rights issues (although a filing of more limited information than would be required in a prospectus is made with the OSC), and distributions made through a stock exchange where sufficient information is provided through the exchange. Quebec has similar provisions, including an exemption from prospectus disclosure requirements for distributions to "sophisticated purchasers." Trades in certain securities are also exempted. In such cases offering documents are not reviewed.

The prospectus contents prescribed under Ontario's Securities Act, which would generally be accepted in the other Canadian jurisdictions, may be summarized as follows: 7/

- Name and jurisdiction of issuer;
- Description of property and business, including development of business in last five years, acquisitions in last two years, and variations in operating results;
- Information regarding directors and officers, their indebtedness, if any, to the issuer, and

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7/ Ontario's Form 12, the form of prospectus prescribed for use by industrial companies, has been used as a basis for comparison. Most of the other jurisdictions require substantially the same information (although sometimes in an abbreviated form) under different names (e.g., Quebec's equivalent is Schedule I).

their interest in material transactions;

- Names of auditors and registrars;
- Plan of distribution and distribution spread;
- Use of proceeds;
- Description of securities offered;
- Principal holders of securities, options on securities, and escrowed shares;
- Risk factors;
- Legal proceedings;
- Prior sales of securities and statement of whether market exists for securities;
- Asset and earnings coverage; and
- Inter-corporate relationships.

Financial statements required in prospectuses are as follows:

- Consolidated income statements for each of last five fiscal years and any part of current year;
- Consolidated statement of surplus for each of such completed fiscal years or part years;
- Consolidated statement of changes in financial position for year covered by income statement;
- Consolidated capitalization table; and
- Consolidated balance sheet not more than 120 days old.

Segment reporting is required and disclosure requirements do not differ greatly from United States requirements, insofar as regular debt or equity offerings are concerned. Much less disclosure may be required in certain circumstances, such as rights offerings. Forecasts are permitted.

Several provinces have adopted a system of integrated disclosure, known as the Prompt Offering Prospectus ("POP") system. 8/ Under the POP System, senior issuers who meet certain requirements including the filing of certain information with the securities commission over a period of 36 months, non-default on debt obligations, and aggregate market value of common stock, may file short-form prospectuses that incorporate by reference the issuer's current Annual Information Form. This form contains substantially all the material that would be included in a prospectus and is filed annually with the relevant securities commission. The short form prospectus must update all information contained in the Annual Information Form. Its principal distinguishing features

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8/ Provision is made for short form prospectuses in Quebec and the Uniform Act provinces (although special rulings must be obtained for access to the POP system in Manitoba and Saskatchewan). Other provinces may accept short form prospectuses prepared in accordance with Ontario's requirements, provided the material incorporated by reference is filed in their jurisdictions.

are much briefer descriptions of the issuer's business and significantly less financial disclosure.

Substantive review begins when a preliminary prospectus is filed with the relevant local securities authority. The preliminary prospectus may be used to solicit expressions of interest. It must contain certificates signed by its CFO and CEO, by two directors, by the underwriter and by the promoter, if any, representing that full disclosure of all facts relating to the securities offered thereby is included. It must be accompanied by certified copies of resolutions of the issuer's board authorizing the prospectus, an auditor's comfort letter (if financials are not included in the preliminary prospectus) and geologists' reports on any material natural resource properties. Material contracts and experts' consents may be filed with either the preliminary or the final prospectus.

Once concerns have been raised and resolved, a final prospectus may be filed and distribution may commence upon issuance of a receipt for the prospectus. Not all offering documents are reviewed by the relevant securities commission. The OSC, for example, does not review the offering document used in exchange offers.

The Securities Act of Ontario expressly empowers the OSC to make certain qualitative judgments on the merits of the securities to be offered by a prospectus. Approval will be refused if the prospectus does not meet the disclosure requirements of the Securities Act. Approval will also be refused if, in the opinion of the director of the OSC, the resources of the issuer are insufficient to accomplish the purpose of the issue as stated in the prospectus, if the issuer cannot be expected to be financially responsible, if there are grounds for believing that the issuer's business will not be conducted with integrity, or if any person or company preparing part of the prospectus is unacceptable. The director may also refuse to approve a prospectus if the director thinks it is not in the public interest to do so.

Similarly, Quebec's director may refuse approval "if the protection of investors requires it." Power to refuse approval of a prospectus is possessed by most of the other local securities authorities under their respective statutes. Saskatchewan, for example, may refuse approval where an "unconscionable" consideration is given for promotion purposes or for the acquisition of property. When concerns are raised about an issuer or its business, it is more likely that additional disclosure, disclaimers or warnings will be required by the reviewing commission rather than that a receipt for a prospectus will be refused outright.

Any person affected by a decision of the director in Ontario is entitled to a hearing and review by the OSC. A decision of the OSC may, in turn, be appealed to the Divisional Court of Ontario. There is, however, a reluctance on the part of the Canadian courts to review regulatory compliance matters in the securities field and deference is paid to the decision of securities administrators. The decision of a securities commission is therefore unlikely to be overturned.

c. Listing Requirements

Issuers apply to the appropriate stock exchange for listing of securities. On the TSE, for example, formal approval is granted by the Stock List Committee. Where a company is going public at the same time as it applies for listing, formal approval on a conditional basis is given, and the applicant must meet the TSE's listing requirements (such as shareholder distribution) upon completion of the public offering.

Each exchange has different listing requirements, which may vary according to an issuer's industrial sector. Listing requirements focus on the capitalization (size of assets or profitability) of the company and the size of its public shareholding. The TSE requires, for example, that a class of securities for which listing is sought be distributed among at least 200 public shareholders, and that the aggregate market value of such securities be at least C$350,000 (currently about US$253,000). Operating companies must show pre-tax profits and emerging companies must have substantial assets and sufficient working capital.

6. Secondary Market

Prospectuses are generally not required for secondary trades (unless, for example, a block of securities representing control of an issuer is traded or the primary distribution was made pursuant to an exemption from the prospectus requirements).

Once an issuer has made an offering of securities, it is obliged to make ongoing, timely disclosure of all "material changes." Reporting issuers must prepare and file with the appropriate securities commission comparative quarterly interim financial statements within sixty days (45 in Quebec) of the end of the quarter, and annual audited comparative financial statements within 140 days of the fiscal year end (90 in Quebec). These statements must be distributed to shareholders.

The stock exchanges' continuing disclosure requirements generally reflect the requirements imposed by the provincial authorities. Issuers who make use of the POP system file Annual Information Forms as described above.

7. Liability

Under the Ontario and Alberta securities acts, civil liability for misrepresentations in prospectuses falls on issuers, selling security holders, directors, underwriters, persons who have given consent to the inclusion of reports by them in the prospectus (in respect of such reports only) and any other person signing the prospectus. 9/ Purchasers of securities are deemed to have relied on such misrepresentations. No liability rests with persons making representations in the prospectus that they believed to be accurate after reasonable investigation, or who previously withdrew their consent to the filing of the prospectus or to the inclusion of such representations.

Quebec imposes liability for misrepresentations upon the issuer or selling security holder, the issuer's senior executives and the dealer through whom such securities were distributed. The defendant is liable for damages unless it can be shown that the defendant acted with prudence and diligence (except where the issuer or selling security holder is the defendant) or that the plaintiff knew of the alleged misrepresentation. 10/

Under the federal Canadian Criminal Code, Part VIII, Sections 338 and 339, it is an offense to use the mails to defraud. This provision has been applied to fraud in prospectuses. Under most provinces' securities acts, any person who makes a misrepresentation in a prospectus is guilty of an offense and subject to a fine and in the case of an

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9/ Section 126, Ontario Securities Act; Section 168, Alberta Securities Act.

10/ Sections 218-220, Quebec Securities Act.

individual, to imprisonment. 11/ Every director or officer of a company who authorized, permitted or acquiesced in such offense is also guilty of the offense and subject to the same penalty. In Ontario, no person can be convicted if he proves that he could not, with reasonable diligence, have known that the statement in question was a misrepresentation.

8. Rating System, Withholding Tax, Limitations on Transferability

There are two bond rating services, the Canadian Bond Rating Service (the "CBRS") and the Dominion Bond Rating Service, Ltd. Both agencies rate domestic commercial paper and corporate bonds. Ratings may vary considerably between agencies. The CBRS also rates governmental issues, which usually are rated in the highest categories.

A standard 25 percent withholding tax is generally applied to dividends and interest, although there are some exceptions, especially in the case of bond interest. Most government and treasury securities and recent long-term corporate bonds are exempt from withholding tax. Withholding tax is reduced to 15 percent for investors in certain countries with which tax treaties exist.

11/ Section 81, Ontario Securities Act; Section 161, Alberta Securities Act; Sections 196, 197, and 202, Quebec Securities Act.

Regulations administered by the Foreign Investment Review Agency were developed to prevent the control of certain Canadian businesses by foreigners. Thus foreigners are restricted in their acquisition of shares issued by companies in, among others, the banking, energy and communications businesses and, until recently, the securities business in Ontario.

Canada has no exchange controls restricting capital movement.

E. FEDERAL REPUBLIC OF GERMANY

1. Description of Statutory Scheme and Regulatory Authority

The West German securities market is relatively unregulated compared to those of most other developed countries. There is no central supervisory body that oversees securities trading. The regulation that does exist is exercised principally over the stock exchanges, leaving trading off the exchanges comparatively unregulated.

Germany has a federal legal system and a federal statute governs the securities market. Pursuant to the Stock Exchange Act, 1/ the governments of the states (or "Länder") are given jurisdiction over the establishment and supervision of stock exchanges in their states. The states appoint commissioners for this purpose. Commissioners attend meetings of the stock exchange supervisory bodies but do not intervene in their operations. There is little federal supervision of the exchanges and, to a large degree, the stock exchanges are self-regulatory. The Stock Exchange Act gives the exchanges jurisdiction over the fixing of prices, the admission of securities to listing, membership of the exchange and the prevention of fraudulent manipulation of securities prices. The exchanges also regulate securities professionals. In

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1/ The Borsengesetz of 1908, as amended. Several decrees and administrative orders relating to the securities market have also been issued by the federal authorities.

order to be licensed, brokers (who perform a more limited function than do brokers in the United States) must meet the exchanges' requirements for personal reliability and professional competence. However, professionals are not subject to the same degree of self-regulation as in the United States.

There are no restrictions on banks' activities in the securities field. Banks obtaining banking licenses may participate freely in securities transactions. No distinctions are made between investment and commercial banks, and all banks may underwrite offerings of securities. Banks also function as intermediaries, accepting brokerage orders from the public; therefore, brokers such as those common in the United States do not exist.

The principal sources of prospectus disclosure requirements are the Stock Exchange Act and the Notification of Admission of Securities based thereon (the Zulassungsbekanntmachung or "ZulBek"). The ZulBek is a Federal Implementing Order issued in 1910. It sets out the duties of the stock exchanges' listing committees and the standards to be applied by them. The provisions of the Stock Exchange Act reflect EEC requirements relating to exchange-traded securities.

The Stock Exchange Act and the ZulBek cover only "official" trading on a stock exchange. Trades made off the exchanges are subject to minimal regulation. Parts of other statutes relating to the operations of issuers engaged in particular businesses also effect the manner in which such issuers may distribute assets. 2/

Because the Stock Exchange Act is applicable only to exchange-listed securities, there is a considerable discrepancy between the extent of regulation of securities transactions made on an exchange, and those made on the "unofficial" market. While the regulation to which exchange-traded securities are subject is extensive (although not as extensive as that of the United States), trading off the exchanges is virtually unregulated. Only for investment funds has a detailed system of control been instituted. 3/

Since Germany has no system of registration and because its prospectus requirements apply only to securities listed on a stock exchange, securities offerings made abroad, whether or not by German issuers, and whether or not to German nationals, are not subject to regulation.

2/ *See, e.g.,* the Stock Corporation Act (Aktiengesetz), which regulates the affairs of stock corporations and partnerships akin to United States limited partnerships, and also imposes periodic reporting requirements. Mutual fund distribution is regulated by the Investment Company Act. It does not cover foreign investment companies, which are subject to the Foreign Investment Companies Act.

3/ Investment funds are governed by the Investment Company Act or Gesetz uber Kapitalanlagegesellschaften of 1957 (the "KAGG").

2. Nature of the Securities Markets

There are eight regional stock exchanges in Germany. 4/ Frankfurt is the most important of these, accounting for about 50 percent of the total turnover on all exchanges. Düsseldorf accounts for a further 30 percent. There are some differences among the practices of the various exchanges. In several cities the stock exchanges are private associations, while in others they are organized by the local chamber of commerce. Two types of dealing take place on the exchanges: "official" and "regulated unofficial" dealing. Officially-listed securities are the only securities for which prospectuses must be produced. The securities of larger companies, government bonds and foreign issuers are officially listed. Transaction prices are published in the Official List and in the press.

4/ These are Berlin, Bremen, Düsseldorf, Frankfurt, Hamburg, Hanover, Munich and Stuttgart. In 1987, the Arbeitsgemeinschaft der Deutschen Wertpapierbörsen, a body representing the interests of these stock exchanges, was created.

Listing requirements are set by each exchange. 5/ Official prices are set by the Kursmaklers. 6/

"Regulated unofficial" dealing takes place on the exchanges between banks and/or Friemaklers. 7/ Listing requirements are less onerous than for official dealing. Smaller companies' securities are traded by this method. Prices are published by the Friemaklers. The regulated unofficial market on all stock exchanges is subject to oversight by a supervisory body established by the eight exchanges.

Unregulated unofficial dealing takes place off the exchanges with unlimited hours. Trading may be literally over-the-counter (many banks will exchange bearer securities

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5/ In order to be listed on the Frankfurt Stock Exchange, the par value of securities to be listed must total at least DM 500,000 (currently about $250,000) (where shares have no par value, at least 1,000 must be listed), the company must have been in business continually and successfully for five years and have a dividend record, and the number of shares available for stock exchange trading should be sufficient to guarantee the proper determination of share price.

6/ Kursmaklers are official brokers who arrange transactions between members and are responsible for the daily setting of prices. They concentrate on securities within specific industry sections.

7/ Friemaklers or unofficial brokers engage primarily in "unofficial" trading among members. Banks, which are also members of the exchanges, provide the link between the public and the stock exchange floor.

for cash) or by telephone. Prices are published by Friemaklers and in private newsletters. Anyone may buy and sell securities in this market, subject to no supervision or disclosure requirements. There is no requirement that trading in listed securities be confined to the listing exchange, and thus all securities may be purchased in the unregulated unofficial market.

A fourth market segment, the "geregelte" or "regulated" market was established in May 1987. The government hopes to encourage medium-sized companies to go public on this market, which is comparable to London's Unlisted Securities Market. Listing on the geregelte market is cheaper to obtain than on the official market, but more disclosure will be required than in the unofficial markets. It is expected that this market will ultimately replace the regulated unofficial market.

3. Issuers

Not all potential domestic issuers make use of the German securities markets. Many larger companies find that fixed-interest bank loans provide capital at more advantageous rates than do bond issues. Equity issues are similarly disfavored. 8/ Since 1983, however, companies have been coming

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8/ Even of those companies issuing securities publicly, a limited number apply for listing. Some 3000 public companies exist in Germany, only 451 of which had an official listing at the beginning of 1986.

to the securities markets in increased numbers. In addition to corporations, non-government issuers include mortgage and commercial banks and other financial institutions.

Foreign issuers make use of the German markets; they often list their securities on the stock exchanges for public relations purposes. Some foreign issuers prefer to raise capital in the unofficial markets by private placements, although official estimates show that foreign issuers prefer the official to the unofficial markets. The number of securities offerings in Germany made by foreign issuers has increased in recent years.

The federal government issues long- and medium-term bonds, as do federal agencies such as the post office and the railways. States, municipalities and cities also issue debt securities.

As of the beginning of 1986, there were 628 companies with equity shares listed on the German stock exchanges. Foreign companies accounted for 177 of this total. Of the listed companies, 15 were newly authorized in 1985 to list their equity on the German stock exchanges, with seven of these being foreign issuers. There were new listings in 1985 of bonds and debentures totalling DM 233 billion ($79,097.2 million), compared to listings of DM 133 billion ($47,293.8 million) on the German stock exchanges in 1984. The domestic private sector accounted for DM 126 billion ($42,849.7 million) of the 1985 total, the domestic government for DM 70 billion ($23,593.2 million), and DM 37 billion ($12,654.3 million) were international bond issues. 9/

4. Types of Securities Traded

Corporate bonds and equities are available, but not actively traded. Less than 0.5 percent of all corporate financing is raised through the issue of shares. 10/ Most equity securities are common shares with voting rights. Disproportionate voting rights are generally not found in securities of the same class. Preferred shares, which carry no voting rights, may be issued. Warrants carrying the right to equity securities are available, as are certificates of participation, which provide participation in profits with no voting rights. Both debt and equity securities are generally in bearer form although partly paid shares must be in registered form.

Corporations may raise capital easily through bank borrowing or through the issuance of debt certificates known as

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9/ International bonds include Eurobonds and foreign bonds.

10/ Turnover in equity securities is increasing more rapidly than in debt securities however.

schuldscheindarlehen, which are not legally classified as securities. These certificates are not listed on an exchange; however, they are traded in a large and active over-the-counter market. Government and bank bonds are the most important element of the German securities market. Most of these are fixed-interest bonds, since floating rate notes were not permitted until 1985.

The so-called "gray" (unregulated unofficial) market is dominated by different kinds of mutual funds, tax loss companies, "public limited partnerships" (which provide tax shelters) and real estate investment trusts. The market in such securities is relatively illiquid.

5. Primary Offerings

a. Participants in a Distribution

Most offerings of securities, whether on the official or unofficial markets, are made through banks. When an issuer intends to offer securities, it contacts a bank which forms a syndicate for sale of those securities. The bank will also act as a sponsor if official listing on an exchange is to be sought for the securities. Syndicate members may act as selling agents or as underwriters.

There are a variety of issuing procedures, but in general public sector bonds are sold through a banking consortium, while private sector bonds are sold directly to the market by the issuing institution without the use of a consortium or intermediary.

Authorization must be obtained from the monetary authorities prior to issue of private bonds. The Capital Market Committee, which comprises representatives of the major issuing houses, consults with the German Federal Bank (the "Bundesbank") on the timing and volume of new issues to ensure an orderly capital market through adoption of a voluntary issue calendar.

All securities are offered to the public through publication of prospectuses in newspapers. There are no restrictions on advertising of any securities, and banks often additionally send offering material directly to their customers by mail. Completion of distribution, including listing, takes about three to four months.

Prospectus requirements derive from listing applications rather than from the nature of the offering. There is no particular legal distinction between public and private issues. Despite the relative absence of regulation, most equity issues are made by private placement rather than by advertisement to the general public.

Individual security holdings are increasing, but Germans are traditionally wary of the stock markets. Nevertheless, individuals, albeit a relatively small number of wealthy investors, make up a large proportion of the investor base, either directly or through mutual funds. Institutions such as pension funds also participate in the market; however, these are often subject to limitations on the type of investments they may make. Foreign investors, principally from Switzerland, Britain, the United States, and Arab countries, play a large part in the market, especially in debt securities.

b. Disclosure and Review

The Stock Exchange Act requires publication of a prospectus prior to listing. No prospectus or equivalent document need be published before a security is traded in the regulated unofficial market although a memorandum summarizing the business position of the issuer must be submitted to the "Committee for Trading Securities Not Officially Listed" prior to trading on the regulated unofficial market. 11/

Prospectuses are not required for securities issued by federal or state government agencies, nor are they required for other issuers if a prospectus has been published within twelve months prior to application for admission of additional securities in which case the issuer need publish only a "notice of referral." Such notice contains all the principal data required in a prospectus, and indicates material changes since

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11/ Although prospectuses are not required, certain minimal information regarding the issuer must nevertheless be disclosed to potential investors.

the date of the last prospectus. It may simply make reference to the financial statements in the last prospectus unless more recent financials have been published, in which case they must be included. Prospectus requirements may be reduced where application is made to list securities already listed on another exchange. With respect to securities traded on the "gray" market, disclosure of information is solely at the promotor's discretion.

Information to be provided in prospectuses covers:

- Name of issuer, registered office, purposes, and in the case of offerings of equity securities, its directors and supervisory board, fiscal year and manner by which notices are given to the public;
- Use of proceeds of the offering;
- Value of securities, amount, series numbers and nature of certificates;
- Rights of securities as regards terminability, redemption (more detailed information regarding rights of securities is required when equity is issued) and rights of the issuer's other securities;
- Security or collateral for debt securities;
- Interest rate, when interest or dividends are payable, deductions or restrictions on payment of dividends or interest;
- Dividend history for the last five years;

- Financial liabilities not apparent from the balance sheet;
- Latest financial statements (no older than 13 months), with explanation of balance sheet items relevant to the issuer's economic position;
- Turnover for the last three years;
- Recent negative developments; and
- Rights of any third party to acquire the issuer. 12/

By law, an investment company's prospectus, which must be furnished to each investor, must provide specific information as to the company's investment policies, terms and time schedule of inventory statements, the company's management fee, the redemption price of the securities and a current list of the company's holdings. 13/

Both the prospectus and the listing application must be published in the Financial Gazette and at least one other principal newspaper. Prospectuses are not reviewed by any

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12/ A "Working Paper," which contains all requirements for the layout of prospectuses and listing, is used by German securities professionals. It is not publicly available. "Working Paper for the Listing Committees at the Stock Exchanges of Berlin, Düsseldorf, Frankfurt am Main, Hamburg, Hanover, Munich and Stuttgart," Spring 1966, status juris: 1974.

13/ Investment funds are governed by the Investment Company Act or Gesetz uber Kapitalanagegsellschaften of 1957 ("KAGG").

regulatory body other than the listing committee of the stock exchange where the securities are to be listed. The draft prospectus must be filed together with copies of the issuer's constitutional documents and other documents relating to the issuer's current liabilities and any litigation or recent material developments.

Although the listing committee is required to ensure that the prospectus is complete, it does not guarantee the accuracy of any information contained in it. The purpose of the listing committee is to ensure that sufficient factual information is given to enable investors to evaluate the securities to be listed. 14/ An application for listing that fulfills the legal requirements cannot be refused unless the public interest would be harmed or admission would "give rise to a deception of the public." The latter allows the listing committee to refuse admission to securities of issuers in financial trouble or grossly overvalued securities. The decision to refuse admission can be appealed to an administrative court.

Repeat issues of securities can be made within a year of issue of a prospectus by a "reference prospectus" which includes essential information about the issuer and its management, details of economic and financial developments and

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14/ Securities traded on the regulated unofficial market undergo a comparable review process, but are subject to less strict disclosure requirements.

the latest annual financial statements. Other information is incorporated from the original prospectus.

6. Secondary Trading

Trading on the exchanges can only be executed by using a bank represented at the relevant exchange. Securities dealing is dominated by banks, which have a legal monopoly on dealing. The largest of the banks are represented at several exchanges.

Continuing disclosure requirements depend on the nature of the issuer and whether its securities are listed. Listed companies subject to the Stock Corporation Act are required to publish annual financial statements and a report by management both in the Federal Gazette and a stock exchange gazette. Financial statements must be audited, and their content is prescribed in detail. Other entities have similar reporting requirements. Investment companies are required to disclose details of their securities holdings twice a year. 15/ Requirements of the EEC Directives on financial reporting are expected to be incorporated into German law shortly.

Issuers of all listed securities (whether or not subject to the Stock Corporation Act) are required by the Stock Exchange Act to undertake, during the period that their securities are listed, to publish notices, annual financial

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15/ KAGG Section 25.

statements and resolutions as to distribution of dividends in the Federal Gazette. In the case of equity or convertible securities there is an additional requirement for publication of this information in at least one stock exchange journal. Financial statements are not required by the Stock Exchange Act to be audited.

7. Liability

Liability for the accuracy and completeness of the information in the prospectus for officially listed securities rests with the issuer and with the banks that are instrumental in listing the securities. These persons are liable to investors for damages proved to have been the result of inaccurate statements made with intent or through gross negligence. 16/ Actions for recovery of such loss are, however, not common. More protection is provided for investors in mutual funds. Under the Investment Company Act, liability

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16/ Section 45, Stock Exchange Act. This section only applies to loss occasioned by reliance on a prospectus that is already published. If, as is common, rights are taken up prior to the publication of the prospectus (German banks often offer rights to securities as yet unissued), the Stock Exchange Act provides no protection against misstatements. Prospectus liability for investment companies is governed by KAGG Section 20, which affords more investor protection in that, unlike the Stock Exchange Act, the burden is not on the investor to prove the issuer's failure to provide accurate information.

for prospectus misstatements is extended to professional dealers neglecting to exercise due diligence.

The Penal Code imposes penalties upon persons damaging another person's financial position by fraudulent misrepresentation. The Stock Exchange Act also provides for criminal penalties for any persons issuing incorrect information in a prospectus or other public announcement with the object of obtaining subscriptions to or purchases of securities. 17/

8. Rating System, Withholding Tax, Limitations on Transferability

There are no domestic rating agencies in Germany similar to those in the United States.

A 25 percent withholding tax on interest and dividend payments on domestic DM-denominated securities was repealed in 1985. A turnover tax of 0.25 percent (0.1 percent for public and certain other bonds) is imposed upon transfer of securities. The government promised in 1987 to abolish this turnover tax.

There are presently no restrictions on foreign ownership of securities, and in 1986, foreigners accounted for more than half the sales of all securities in Germany. Historically,

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17/ Section 88(1), Stock Exchange Act.

however, the government's attitude towards foreign investment has been encouraging or restrictive as necessary to support the DM.

F. FRANCE

1. Description of Statutory Scheme and Regulatory Authority

a. Source of Regulation

France's scheme of securities regulation is supervised by the Commission des Operations de Bourse (the "COB") and the Chambre Syndicale des Agents de Change (the Stockbrokers' Council or "Chambre Syndicale"). Securities may not be offered and sold publicly by most issuers 1/ in France without approval of the COB. Where securities are to be listed on a stock exchange or traded on the over-the-counter market, approval of both the COB and the Chambre Syndicale is required. The Treasury Department of the Ministry of Economy supervises, *inter alia*, exchange control, cross-border investments and securities markets, and coordinates large offerings and the issue of foreign securities. The COB, an independent regulatory agency, was created in 1967. It consists of a chairman appointed for a four-year term by the Council of Ministers (the Cabinet), four members appointed for four-year

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1/ The original legislation applied only to companies limited by shares but was subsequently expanded to cover investment companies and real estate investment companies. Although few such exist, issuers with a different form of corporate organization would not be subject to disclosure requirements. Similarly, although few bonds are issued by borrowers other than companies, such issuances are not subject to COB supervision at the time of issue, but only upon application for stock exchange listing.

staggered terms by the Finance Minister, and a government representative, together with a full professional staff.

The COB's purpose is to protect investors by, among other things, requiring disclosure of adequate information and ensuring the proper function of the financial markets. To this end, it regulates the information given by issuers to their security holders and the public in general. It also oversees such matters as the disclosure of acquisition of control by security holders and the operations of the stock exchanges. Additionally, the COB processes complaints regarding the operations of the securities markets, and regulates insider trading, which is illegal.

The body of disclosure requirements administered by the COB is found in various laws passed by parliament, decrees implementing such laws and administrative orders. Provisions relating to exchange-listed securities are based on the requirements of EEC Directives. Trading on the stock exchanges is limited to stockbrokers ("agents de change"), who may buy and sell only for clients, and not for their own account. All stockbrokers belong to a self-regulatory organization, the Compagnie des Agents de Change ("CAC") whose regulations are legally enforceable by the Finance Minister and are subject to approval by the COB. The CAC regulates examinations of agents de change and oversees their capital requirements.

Agents de change, whose numbers are limited by law, are licensed by the Finance Minister after passing professional examinations and meeting the approval of the Chambre Syndicale. There is no direct government regulation of stockbrokers, although the COB supervises the activities of auditors, investment advisers and "remisiers" (intermediary brokers).

CAC members elect the members of the Chambre Syndicale. Its powers and organization are determined by governmental decree. 2/

b. Scope of Regulation

While the filing and disclosure requirements for all public issues are similar to those in the United States, the requirements apply only to certain types of issuers and only to sale of securities for cash. A sale of securities by certain issuers, 3/ or by any issuer for consideration other than cash, is not subject to the regulatory system. The regulation of securities professionals is also similar to the United States system, although supervision is somewhat less strict.

The investigative powers of the COB are limited to the activities of companies publicly offering their securities in

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2/ The Decree of October 7, 1980 (as amended) is the principal enabling law.

3/ *See* discussion in n.1, *supra*.

France. 4/ Offers made outside the French markets, whether or not to French citizens, are not subject to regulation.

2. Nature of Securities Markets

France has seven stock exchanges, located in Paris, Bordeaux, Lille, Lyon, Marseilles, Nancy and Nantes. The Paris Bourse (Stock Exchange) is, however, clearly dominant, with some 98 percent of all trading in listed securities being conducted there. The regional stock exchanges tend to trade securities of local interest only. Each stock exchange comprises three different markets: the official stock exchange, the second market and the over-the-counter market. These are described more fully below.

By law, a given security may be traded only on one market. Listed securities must thus in principle be traded only on the stock exchanges, although off-exchange trades are allowed in certain cases, subject to approval of the Chambre Syndicale if a stockbroker is used. An example of such a case would be a transaction between companies of the same affiliated group, or between two individuals "who know and have confidence in each other". The issuer of a security must give its approval for

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4/ Regarding the concept of a public offering, see discussion accompanying n.11, infra.

block transactions in that security to be consummated off the exchange.

The COB decides whether a company should be admitted to the Paris or regional exchanges, taking into account the location of the company's activities and the expected market for the shares being listed. Admission requirements for the regional exchanges are similar to those of the Paris Bourse, with reduced requirements in such qualification categories as the minimum number and market value of the issuer's securities.

The Paris Bourse is the sixth largest market in the world, with a market capitalization of approximately FFr 2,162 billion (currently about $335 billion), approximately 30 percent of which is equity. 5/ In order to list on the Paris Bourse, the Chambre Syndicale requires a company to have had profits and have paid a dividend in its last three fiscal years. The estimated market value of the company's shares should be "adequate." Although there are no fixed criteria to determine in practice what is meant by "adequate," a minimum value in the range of FFr 200 to FFr 300 million (currently about $30 to $46 million) is usually required. The COB requires that at least 25 percent of the share capital be offered for sale to the public and that the share capital consist of at least 320,000 shares. Foreign companies are subject to the same

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5/ 1986 OECD figures.

requirements, except that there is no fixed minimum number of shares.

Securities listed on the official stock exchanges are quoted either on the marché du comptant or on the marché à règlement mensuel (previously the marché à terme). Securities quoted on the marché du comptant are generally delivered and paid for at the time of the transaction. This differs from the usual practice regarding securities quoted on the marché à règlement mensuel, where, at the time of a transaction, the seller and purchaser of the securities generally agree to tender the securities and the agreed consideration at a fixed date in the future.

The Second Marché, or second-section market, was created in 1983 to provide access to the capital markets for medium-sized companies. Listing requirements on the second-section market are less onerous than those of the Bourse, and the market acts as a testing ground for companies that intend to apply for full listing at a later date. As of the end of 1985, about 130 securities, four of which were foreign, were listed on the second-section market. Aggregate market capitalization is about FFr 60 billion ($7.9 billion).

Liquidity in the second-section market is good as the banks responsible for bringing issuers to the market are obliged to maintain markets in those issuers' securities. The second-section market is attractive to family-owned companies wishing to raise capital but not wishing to comply with the requirements for full listing. For example, the second-section market requires that only 10 percent of a company's capital be distributed to the public, while the Bourse requires that 25 percent of the listed company's capital be distributed to the public.

The over-the-counter market ("marché hors-côte"), exists for securities not listed on the "marché officiel" (i.e.- the main section of the exchanges) or on the second marché. Liquidity on the marché hors-côte is poor. Volume in this market is much smaller than on the official exchanges, especially in Paris, where it is very limited.

3. Issuers

Government as well as private agencies issue debt and equity securities. A number of foreign issuers, principally British, United States and Japanese, have introduced securities to the French markets, and eleven of the fourteen new equity issues listed in 1985 were by foreign companies.

As of the beginning of 1986, there were 678 companies with equity shares listed on the Paris Bourse. Foreign companies accounted for 189 of this total. There were new listings in 1985 of bonds and debentures totalling FFr 311 billion ($39,366.4 million), as compared with listings of FFr 232 billion ($24,741.1 million) on the Paris Bourse in 1984. The domestic private sector accounted for FFr 70 billion ($8,930.5

million) of the 1985 total, and the domestic government for FFr 240 billion ($30,435.9 million).

4. Types of Securities Traded

For a variety of reasons, the most important being favorable banking regulations, companies have historically preferred to borrow from banks when seeking new capital, rather than to issue securities. The securities market in France is therefore small compared to the country's industrial base. The securities market has improved significantly in recent years in terms of turnover and liquidity, 6/ however, and the range of securities available in the French markets is nearly as wide as that in North America. New debt and equity instruments have been devised in order to attract all kinds of investors. This is due to recent legislation which has enabled companies to issue many new types of securities so long as certain minimal requirements are met. 7/

In terms of capital value and turnover, the debt market is about four times larger than the equity market. Although trading in both is increasing, tax considerations and issuers'

6/ Liquidity has been promoted by government restriction on French persons' investment abroad.

7/ Law Nos. 83-1 of 3 January 1983, and 85-1321 of 14 December 1985.

aggressive pursuit of the longer-term debt market have resulted in the more rapid increase of debt security trading. An interesting feature of the French market is the availability of index-linked bonds. 8/

Other securities available include interests in mutual funds. French investors have access to over 2,000 funds, the number of which has increased dramatically over the last five years. They are managed by banks and stockbrokers. Assets held by mutual funds totalled over FFr 194,121 million ($26 billion) as of December 31, 1985. Options are available and traded on many securities. A formal market for traded options was introduced in 1986. Preemptive rights issues are common on the Paris Bourse.

The current deregulation of the French financial markets has led to the introduction of new securities such as non-voting preferred shares and subordinated certificates of indefinite maturity. 9/ A limited form of disproportionate voting rights (shares with double votes) is permitted under certain circumstances. Attempts are also being made to widen

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8/ These bonds, the redemption and/or interest payments of which are linked to the value of other monetary indices, such as gold or the value of the European Currency Unit, provide useful protection against the effects of inflation and the weakness of the French franc.

9/ These are the functional equivalent of non-voting equity participation securities.

access to short-term debt securities for investors other than financial institutions.

Bearer securities are popular because of the anonymity they provide. Debt securities are usually issued in bearer form, although registered bonds are also available. Equity securities are available in both registered and bearer form.

5. Primary Offerings

a. Participants in a Distribution

The distribution of securities is usually carried out by a bank or banks appointed by the company. Such banks normally act as selling agents only, not as underwriters. Banks, whether investment or retail, are not restricted from securities activities, and are an important link to French brokers.

The terms and conditions of each issue are set by joint agreement between the issuer, lead manager and the Treasury Department a few days before the official opening of the issue. The banks prepare and co-sign the company's prospectus. The distributing banks make the offering to the public and to institutional investors (such as insurance companies and pension funds) as well as to other financial institutions. Distribution to the public (usually wealthy private customers) is done by the banks through their own branches, and through brokers. 10/

Public advertisement is permitted only when specific approval is obtained. Notice of a public offer must generally be inserted in the official legal bulletin, however. Stock Exchange quotation occurs the day before the issuer receives the proceeds of the offering, which is usually about two to four weeks after the official opening of the issue.

b. Disclosure Requirements

The type of disclosure to be made by an issuer and the review to which that disclosure is subject depends on whether the securities being issued are to be offered publicly and whether a stock exchange listing or hors-côte trading is to be sought for them. A prospectus approved by the COB is required before any securities, domestic or foreign, may be offered to the public. 11/ A file with information about the issuer's

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10/ France has a low percentage of individual share ownership. Only 1.5 million people out of a population of over 55 million hold shares. Debt security ownership is more comparable to other industrialized countries. Additionally, around 5 million people own shares in mutual funds.

11/ Articles 6 and 7, Order 67-833 of Sept. 28, 1967. The law characterizes as a public offering that which satisfies any of the following criteria: (1) the securities issued by the company are admitted to the official stock exchange quotation, (2) the company (continued . . .)

business and prospects, and a copy of the draft prospectus are sent to the COB and, when listing of the securities is sought, to the Chambre Syndicale as well. Additionally, any offerings of securities by foreign issuers and those by domestic issuers for amounts above FFr 15 million (currently about $2 million) must be approved by the Finance Ministry. In such a case, the Finance Ministry will consult the COB prior to approval of the securities.

The prospectus must be given to any person invited to subscribe for securities. 12/ Prospectuses, the contents of which are prescribed by a COB Instruction of February 2, 1982 (the "COB Instruction") cover the matters set out below. It should be noted that the COB Instruction provides guidelines rather than a format which must be followed strictly, and that prospectuses for second marché, hors-côte or unlisted

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(. . . continued)
sells its securities through the services of banks or related establishments, or stockbrokers, or (3) the company advertises, in any way, the securities it wishes to sell. (Arts. 71 and 72, 1966 Act). These criteria are not exhaustive, and the COB assumes an offering is public unless proved otherwise. Only certain companies that issue shares (sociétés par actions) are permitted to make public offerings.

12/ Prior to 1967, disclosure was limited to a requirement that details of the issue be published by a "statutory note" in the official gazette. The statutory note has lost a great deal of importance since 1967, but the requirement has been retained. One of the reasons for this is the desirability of centralizing all company announcements in one publication.

securities tend to be shorter and less detailed than those for securities listed on the marché officiel. 13/

Prospectuses for all securities must include the following information:

- Corporate resolution concerning issuance of securities, offering price;
- Information concerning shares including number, par value, class, rights to current earnings, exercise of pre-emptive right, period open for subscription, banks where subscription can be made;
- Information concerning debentures including dates at which is interest payable, interest rate, effective return to subscriber, amortization, repayment, taxation, guarantees, paying agents and details regarding conversion;
- Costs of issue and net proceeds;
- Name, registered office, term of existence, corporate form of issuer, any applicable special statutory provisions, where documents are available;
- Fiscal year, allocations of profits, general meetings, restriction on sale of shares and any other special characteristics;

13/ Art. 112, Règlement Générale de la Compagnie des Agents de Change.

- Capital structure, types of shares issued, convertible debentures, if any, treasury or "founders" shares, changes in capital over past five years, approximate number of shareholders, shareholders owning over five percent, holdings of management;
- Issuer's activities, a brief history, existence of group, if any, number of employees, place of business, principal investments in last 5 years, sources of supply, research and development, types of activity, brand names, volume of sales over 5 years by line of business and with percentage changes, customers and markets, exceptional events and litigation, subsidiaries, and, if the company is part of a group of companies, information must be given regarding the parent, if applicable;
- Management, names and duties of directors and principal officers, and profit sharing and stock options;
- External auditors;
- Recent changes and prospects of issuer;
- Purpose of the issue; and
- Identity of persons assuming responsibility for the prospectus.

Prospectuses for listed securities also include the following matters:

- Description and number of securities;
- Exchange where listed and date of original listing;
- Minimum offering price and justification therefor; and
- Prices on other exchanges.

Prospectuses for unlisted securities must also include the following:

- Market for the securities and return on investment.

As with many non-United States prospectus requirements, information about management is limited. Some textual discussion of industry segments is suggested.

Financial information disclosed in prospectuses covers the following:

- When the company is parent of a group, financial statements of major affiliates for last three (may go up to five) years, consolidated financial statements for last three years, chart showing consolidated source and application of funds;
- Profit and loss statements for last three years, whenever possible with results by division and comments concerning variations, impact of capital gains, if any, and brief description of computation of taxable result;

- Balance sheet for last three years, interim midyear statement and comparison with previous year;
- Non-balance sheet items such as guarantees or leasing contracts; and
- Five year chart showing source and application of funds.

Industry segment information is given "wherever possible," but geographic segment information is not required. The COB requires that issuers submit their accounts to an audit prior to issuance of securities. Audits are performed by statutory auditors authorized by the COB until such time as the COB determines that the quality of the audit carried out by issuers' regular auditors is satisfactory.

Where the securities to be issued are not to be listed, the issuer, usually through a sponsoring bank, submits certain documents to the COB. These documents will include the issuer's constitutional documents, its annual reports, descriptions of the issuer's activities, and the draft prospectus. The COB reviews prospectuses for adequacy of disclosed information, but makes no judgment on the economic soundness of the proposed investment. It may request additional disclosure to be made in the prospectus.

Upon a finding that satisfactory disclosure is made, the COB's stamp or "visa" is attached to the prospectus. The COB has the power to refuse to approve a prospectus, in which case a very limited power of appeal is allowed to the Council of State. The COB does not, however, generally refuse to approve prospectuses, but instead requires amendment of the disclosures made therein.

Where securities are to be listed on a stock exchange 14/ or traded on the marché hors-côte, both the COB and the Chambre Syndicale must approve the issue. The issuer files with the Chambre Syndicale the same documents as filed with the COB, plus a listing application. Approval for the issue of listed securities may take up to five months.

Continuous issuers are often authorized upon application to the COB to use an abbreviated form of prospectus if, in the opinion of the COB, the company generally discloses adequate financial information, such as timely filing of its annual reports, which contain such information. The COB has also allowed under limited circumstances a summary prospectus or "note abregé" to be distributed to investors where a full formal prospectus may be too technical to be understood readily, although the full prospectus must be made available to investors upon request, and sent to securities professionals.

14/ Disclosure requirements and the review process are the same whether application is made for full or second-section listing.

6. Secondary Market

a. Participants

Nearly all securities transactions require the intervention of a stockbroker. More than 75 percent of all securities orders are transmitted to brokers through banks. 15/ The banks also provide services to investors such as safekeeping, collection of dividends and interest, portfolio advice and provision of mutual funds. It is estimated that 50 percent of securities trading is by institutions, and that foreign investors account for 20 percent of trading volume. Reforms aimed at modernization of the secondary market have been instituted recently. The measures adopted have the aim of the provision of hedging protection, more flexible brokerage rates and the gradual introduction of continuous trading.

b. Continuous Disclosure

French corporation law provides that all shareholders are

15/ Brokers are not generally used by the average French investor, who has traditionally been wary of investment in the securities markets. The government is actively trying to encourage greater participation in the markets by small investors.

entitled to receive certain corporate information. 16/ Shareholders may read and copy at the company's registered office documents relating to a company's financial statements, inventory, names of directors and statements of the amounts paid to the ten most highly compensated employees, as well as minutes of shareholders meetings. Prospectuses are not required, however, for secondary trades.

Additionally, companies listed on an official stock exchange must publish in a legal newspaper, prior to their annual meeting of shareholders, the following documents:

- Financial statements for the most recent fiscal year, clearly stating that these are unaudited;
- List of portfolio holdings, with a breakdown by issuer of securities held and value thereof;
- Proposed allocation of profit or loss; and
- Consolidated financial statements, if available.

Within 45 days of the annual meeting, the audited consolidated financial statements must be published in final

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16/ The contents of the information to be supplied annually to shareholders used to be defined in various statutes. Recent changes in the law, however, will phase in requirements regarding disclosure of certain financial information including statements of current net assets, statements of financial position, provisional financing plan and operating statements.

form in the appropriate legal newspaper. A further statement of activity and results must be published every half-year, and trading figures must be published quarterly. Listed issuers have a general obligation to disclose information likely to affect the trading of their securities.

Somewhat different standards apply to companies not listed on an official stock exchange but which have assets of FFr 20 million (currently about $3 million) or more, a securities portfolio in excess of FFr 2 million (currently about $300,000) or 50 percent or more of the capital of which is owned by a listed corporation. These companies must publish in a legal newspaper within 45 days of their annual shareholders meeting their audited financial statements for the most recent fiscal year, the allocations of their profit or loss and their portfolio holdings.

7. Liability

The general principles of liability under tort law apply to actions for misstatements or omissions appearing in a prospectus. Such actions are much less common in France than in the United States.

Both the Penal Code and the Ordinance of 28 September 1967 (as amended by the Law of 3 January 1983) contain provisions forbidding the intentional dissemination of false information relating to the securities of an issuer in order to influence the price of such securities.

8. Rating System, Withholding Tax, Limitations on Transferability

Bond issues in the French market are differentiated according to the quality of the issuer and divided into two categories. First category bonds are issues made by government agencies or public sector corporations regarded as having the same creditworthiness as state issuers. Second category bonds are issued by private corporations and are regarded as having a lower quality than government sector bonds. Partly as a result of the creation in early 1986 of a domestic commercial paper market, the French rating agency, Agence d'Evaluation Financiere recently was formed. 17/ In addition to commercial paper, the agency has indicated that it will rate domestic company bonds in the future.

Interest on government bonds is paid without withholding tax. Interest on other bonds, with certain exceptions, is subject to 10 percent withholding. Withholding from dividends is 15 percent. Stamp tax of 0.3 percent is payable on all

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17/ The agency is owned by insurance companies and other state and private financial institutions.

transfers of securities other than short-term bonds (defined as those having a maturity of less than 7 years).

There are no restrictions on nonresidents' trading in securities in France, although a nonresident may not own more than 20 percent of the capital of a listed French company without permission from the Finance Ministry.

9. Recent Developments

France's securities markets are presently undergoing deregulation as the recently-elected government, in which conservatives and socialists share power, denationalizes state-controlled industries and attempts to create a new base of individual shareholders in the market. One result of deregulation is the increasing regulatory role being played by the COB and the Stockbrokers' Council. As a result the government has deferred more regulatory decisions to financial experts in those organizations.

G. AUSTRALIA

1. Description of Statutory Scheme and Regulatory Authority

Australia is a federation of six states and two territories. The legislative system comprises the state and territorial legislatures together with that of the Commonwealth of Australia. The states, territories and the Commonwealth each have authority to enact securities and companies legislation. The need for uniformity in such laws led to an agreement between the states and the Commonwealth in 1978 (the "Formal Agreement") whereby the Ministerial Council for Companies and Securities (the "Ministerial Council") and the National Companies and Securities Commission ("NCSC") were established by the National Companies and Securities Commission Act 1979. Pursuant to the Formal Agreement each state or territory adopted companies and securities legislation substantively identical to that adopted by the Commonwealth. 1/

1/ The Commonwealth exerts jurisdiction in this respect only over the Australian Capital Territories. The Northern Territory is not a party to this scheme. The legislation adopted by the Commonwealth pursuant to the Formal Agreement consists principally of the following acts:

National Companies and Securities (Commonwealth) Act 1979;
Companies (Acquisition of Shares) Act 1980;
Securities Industry Act 1980;
Company and Securities (Interpretation and Miscellaneous Provisions) Act 1980;
Companies Act 1981; and
Several ancillary Acts, together with Regulations under each Act.

(continued . . .)

The states and the Commonwealth have agreed not to amend such legislation without the approval of the Ministerial Council. The Ministerial Council, comprising representatives from each state, is the sole body responsible for proposing companies and securities legislation. The NCSC has no rulemaking authority and is responsible to the Ministerial Council.

The eight-member NCSC, which came into operation in 1981, is the agency primarily responsible for administering all the state and Commonwealth securities legislation. Most of its powers, however, including the review of prospectus disclosure, are delegated to the Corporate Affairs Commissions ("CACs") of each state.

Securities are not "registered" prior to distribution, as in the United States, but instead a prospectus must be filed with the reviewing authority. Prospectus disclosure requirements in each jurisdiction derive from the Companies Code as well as from regulations adopted by each jurisdiction. If the securities are to be listed, the additional requirements of the Australian Association of Stock Exchanges ("AASE") must be met.

(. . . continued)
This legislation forms the basis for the state acts. The standard form in which the Companies Act 1981 is adopted by all the states is referred to herein as the "Companies Code."

The Ministerial Council approves the establishment of stock exchanges. The Formal Agreement gives the nine Australian stock exchanges substantial responsibility for the regulation of their own and their members' affairs, subject to NCSC oversight. Stock exchange rules are approved by the NCSC.

No person may deal in securities 2/ without a license issued by the NCSC under provisions of the Securities Industry Act 1980. Investment advisers are also subject to licensing. The activities of stockbrokers are self-regulated through the stock exchanges.

While all public offerings of securities are subject to government regulation, the disclosure required by the Companies Code and state regulations is not detailed. The NCSC tends not to become involved in questions of disclosure until a problem has arisen.

The regulation of stock exchanges and securities professionals is similar to the United States model, in that self-regulatory organizations (the exchanges) administer rules that are subject to regulatory agency (NCSC) approval. However, regulation is not as extensive as in the United States.

The statutory scheme covers all offerings of securities made in Australia. Only Commonwealth legislation has full

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2/ The definition of a security is broad; there are, however, several exceptions for certain types of instruments.

extra-territorial operation outside Australia (in cases of fraud, for example). It is not clear on the face of the legislation whether an offer of securities solely to persons outside Australia is required to comply with the disclosure and filing requirements outlined below. The question of jurisdiction of one state over offerings made from that state solely to persons in another state has not been addressed to any extent, principally because most listed companies are listed on all exchanges.

2. Nature of the Markets

Australia has nine stock exchanges. 3/ The Sydney and Melbourne exchanges are the largest, accounting for 95 percent of securities turnover. In terms of market capitalization, the Sydney Stock Exchange is the seventh largest in the world. It is much smaller than the leading world exchanges, however, and Australia's capital markets account for only 2 percent of world market capitalization.

The AASE regulates the operations of the six principal stock exchanges. It was formed in 1937 to adopt and maintain uniform regulations for the listing of securities on each

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3/ Sydney, Newcastle, Melbourne, Ballarat, Bendigo, Adelaide, Brisbane, Perth and Hobart.

exchange. 4/ Since 1972 the exchanges have implemented a policy of "national" listing under which all companies listed on one AASE exchange may be listed on the other five with little additional burden. Companies seeking quotation designate a "home exchange" (usually the exchange in the capital of the state where the company has its principal place of business), but may apply to be listed on more than one exchange. 5/ Technical links between exchanges, including computer quotation systems, are at an advanced stage. Screen trading and automatic settlement are planned. Listed securities may be traded off the exchanges.

Second Boards, first established by the Perth Stock Exchange in 1984, and now operating in Melbourne, Sydney, Brisbane and Adelaide, allow small firms to raise capital publicly without the expense and burden of obtaining a main

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4/ The AASE Stock Exchanges are Adelaide, Brisbane, Hobart, Melbourne, Perth and Sydney. AASE regulations require that companies seeking official listing of their securities have at least 300 shareholders (25 holders in the case of debt securities), that members of the public hold a minimum number and percentage of securities, and that the total value of the securities to be listed be A$300,000 (currently about US$194,800) for equity, A$500,000 (currently about US$324,700) for debt securities. Additional requirements apply to foreign issuers. For example, at least 200,000 shares must be held by at least 200 Australian residents.

5/ The ability to trade on all stock exchanges has prompted discussions concerning the formation of a single national stock exchange.

board listing. 6/ Second Boards permit voting structures that allow founders to keep control of their companies even with a minority of the total equity. As of September 30, 1985, there were about 70 Second Board listings although some of these were accounted for by companies with multiple listings.

Australia has no established market system for the trading of securities not listed on a stock exchange. Such securities must in practice be traded through a stockbroker, or by contacting the secretary of the corporation issuing such securities. There is, however, an active market in debt securities that is conducted between companies as principals, or, to some extent, through dealers or brokers as intermediaries. Securities issued in unit trusts and similar investment vehicles typically must be repurchased by the trust manager under the terms of the trust, rather than traded in the secondary market.

3. Issuers

Issuers of listed securities include both government and "semi-government" (autonomous public sector) entities, although these are outnumbered by private sector issuers. Companies

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6/ Second Board Listing requirements vary. Perth requires capitalization of A$10 million (currently about US$6.5 million), whereas Brisbane requires capitalization of A$20 million (currently about US$13 million).

registered under the Companies Code as public companies may raise capital by sales of debt or equity securities to the public and are allowed access to both the listed 7/ and unlisted markets. 8/ "Proprietary" companies 9/ may not raise capital publicly on or off the stock exchanges.

As of the beginning of 1986, there were 1,095 companies with equity shares listed on the Australian stock exchanges. Foreign companies accounted for only 26 of this total. Of the listed companies, 109 were newly authorized in 1985 to list their equity on the various exchanges, with eight of these being foreign issuers.

4. Types of Securities Traded

Government bonds and private companies' debt and equity securities (all of which must be in registered rather than

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7/ Private sector issuers listed on the AASE exchanges as of June 30, 1985, consist of industrial companies (629), mining companies (256), oil companies (104) and trusts (27). (Official Lists of Capital City Stock Exchanges).

8/ These include both the Second Board and unofficial markets.

9/ Proprietary companies are those registered as such under the Companies Code. Their articles of association restrict membership to 50 persons other than employee-members and restrict the free transferability of their shares. They must raise capital from their members.

bearer form) are available on all exchanges. 10/ Dual class capitalization is permitted, and many variations in voting rights exist. Exchange traded options are available on a market located within the Sydney Stock Exchange.

Unit trusts are common in Australia. These are similar to mutual funds, but due largely to favorable taxation treatment, have extended beyond the type of fund that invests in other securities commonly found in other countries. Property trusts invest in real property, for example, and several trusts have been formed to conduct business operations. Interests in unit trusts and other investment vehicles (for example, bullion investments, franchising plans or afforestation schemes) are defined as "prescribed interests". Investors in prescribed interests do not have the same rights and protections afforded to shareholders (for example, voting rights and election of directors), thus fuller disclosure is mandated (*see* discussion below) and a trust deed setting out the protections afforded investors must be registered with the NCSC.

10/ Most Australian companies are fairly small, and their shares relatively illiquid compared to United States companies.

5. Primary Offerings

a. Participants in a Distribution

Stockbrokers, merchant (investment) banks, and trading banks 11/ all participate in the distribution of securities. Underwriters are usually stockbrokers or merchant banks (usually the latter in debt issues) and may accept the issue on either a best efforts or a firm commitment basis. The lead underwriter may organize a network of sub-underwriters such as merchant banks, stockbrokers and insurance companies.

Usually, when underwriting is on a firm commitment basis, the underwriter places the entire issue with investors prior to listing. Distribution in a best efforts underwriting typically takes longer. No offer or invitation to acquire the securities can be made prior to filing of the prospectus, although in practice the market acquires considerable information about the issue prior to filing. Preliminary prospectuses are not used.

Advertising of securities (particularly before filing) is restricted. Only factual information may be set out in advertisements and other restrictions apply, although relief from certain of the restrictions frequently may be obtained upon application to the NCSC. Occasionally, full prospectuses

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11/ All three of Australia's private trading banks have bought into stock brokerage firms.

are published in newspapers, but more often advertisements will invite readers to apply for a prospectus. Second Board issuers frequently use advertisements in newspapers to sell their securities directly to investors. The most common way in which securities are distributed, however, is by stockbroker placements.

Typical purchasers of securities include banks, insurance companies, stockbrokers and financial institutions. Superannuation or pension funds are thought to be the most important investors, providing a large and growing pool of investment funds. They tend to favor long-term growth securities such as public securities and long-term debt. Insurance companies generally favor more liquid investments. While about 42 percent of available equity securities are owned by individuals, such individuals make up only four percent of the population -- a much lower rate of share distribution than in other developed countries -- and tend to be retirees and wealthy speculators. Employee share ownership is being actively encouraged by the government, apparently with some initial success.

b. Disclosure and Review

A prospectus must be registered before any offer of securities is made to the public. 12/ Exceptions from the prospectus requirement are provided for government issues; for bona fide offers or invitations to enter into an underwriting agreement; to persons in the business of buying and selling securities; to holders of prescribed interests made available pursuant to an approved deed and in relation to that interest; and to existing security holders (although the AASE requires disclosure of certain information on rights issues).

Prospectuses must include the following information:

- Financing plans, including minimum amount necessary for property to be purchased, if any, expenses and

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12/ Section 96(1), Companies Code. The Companies Code does not regulate non-public offers. There is no judicial interpretation of the meaning of "offer to the public". The Companies Code provides that offers to any "section of the public", however selected (*e.g.*, as previous clients of the distributor), are offers to the public. However, the Code does not define a "section of the public". The NCSC considers that any offer to persons who do not have a close business or personal relationship with the offeror is public. In the leading case on the meaning of public offers, the High Court held that whether an offer was public depended on the circumstances of the case. The factors to be considered are the relationship between members of the offeree group, the number of persons comprising the group, the relationship between offeror and offerees, the nature and content of the offer, the significance of any particular characteristic which identifies the members of the group and any connection between that characteristic and the offer. *CAC(SA) v. Australian Central Credit Union,* 5 A.C. 752 (1985). The High Court expressly declined to follow the United States Supreme Court's decision in *S.E.C. v. Ralston Purina Co.,* 346 U.S. 119 (1953).

commission, money borrowed for the foregoing, working capital, and sources of other financing;

- Details of any guarantees by parent corporation;
- Statement that no securities will be issued on the basis of the prospectus later than six months after its date of issue;
- Voting and dividend or capital rights attached to securities;
- Date of any expert's reports included in whole or part;
- Details of material contracts (outside ordinary course of business or which must be described in order to prevent prospectus being misleading) entered into within last two years;
- Auditors' names and addresses;
- Details of nature and extent of interest of every director, proposed director or expert in the promotion of the company or the property proposed to be acquired (applicable only to companies within first two years of incorporation);
- For foreign companies, details of constituent documents and legislation under which incorporated, address of registered office in jurisdiction (if new to Australia), and where and when incorporated;
- States and territories in which prospectus is to be issued; and

- Whether application has been made for stock exchange listing, and upon what exchanges.

Specific textual disclosure of segment information is not required. It is not normal practice to disclose details of individual directors' remuneration. While there is no specific requirement to describe the nature of the issuer's business, in practice a prospectus will not be registered unless it adequately informs investors as to the issuer's business. The NCSC and the CACs have discretion to require issuers to include additional material in prospectuses, and frequently make use of this power.

The Companies Code and regulations thereunder require the prospectus to contain a report by a registered company auditor (a fully qualified accountant who must also meet practical experience requirements and standards of fitness and propriety) covering:

- Statement of profit and loss covering five previous years (and any part of current years for which accounts made up), unless accounts are not made up for any of these years, in which case a statement to that effect is required;
- Directors' report on material changes after date of accounts;
- Assets and liabilities as of the end of the last

fiscal year;

- Dividend history for last five years;
- Estimated payments due to and from subsidiaries;
- Amount payable on application and allotment of each share;
- Information as to previous share offerings in last two years;
- If property is to be acquired with proceeds, details of transaction and previous dealings with such property or its vendor;
- Commissions paid in last two years, and whether directors or promoters received any such commissions;
- Preliminary expenses, and by whom paid;
- Payments to promoters in last two years; and
- If debentures are to be issued, restrictions on issuer's borrowing; amount of subscriptions sought; whether charges can be made over assets that secure deposits or loans ranking in priority or pari passu with the offered securities.

Where the issuer is a member of a group, it may choose to present the group's accounts in consolidated or separate form, so long as the form used gives a true and fair view of the group's accounts. The basis of accounting adopted must be disclosed. Segment revenue and results and other items of information are required in the financial statements of all companies with significant industry and geographical segments under the Australian Accounting Standards ("AAS"). There is no obligation to prepare accounts in accordance with AAS, but in practice the NCSC requires an explanation where AAS requirements are not met. The AAS are prepared by the two professional bodies representing accountants in Australia, using the requirements of the International Accounting Standards Committees ("IASC") as a minimum basis. AAS requirements therefore meet or exceed IASC standards. 13/

Where listing is sought, companies must also comply with AASE requirements, which complement and extend the statutory requirements (and which are fairly uniform, although individual exchanges may impose additional requirements). AASE requirements are as follows:

- Experts' reports must be included in full, must state the experts' qualifications, and may not be included if experts have interests in the property or potential property of the company in which they report;

13/ The principal differences between Australian and United States accounting practices are: (a) fixed assets are sometimes revalued, (b) properties are not depreciated, and (c) surpluses and losses on realization of fixed assets can be included both "above and below the line" under Australian practices. Additionally, United States companies usually are required to disclose a greater amount of information (*e.g.*, pension funding).

- With respect to debt securities, the prospectus may not state on its cover that the issue is guaranteed unless an adequate description of the guarantee appears; and
- Where unsecured notes are offered, the names of all subsidiaries of the borrower that are not guarantors must be given, and reference must be made to the way in which liability limitations are calculated, the assets and liabilities of the borrower and its subsidiaries, and of the guarantor companies, showing advances to and from guarantor and non-guarantor subsidiaries, reference to the fact that in winding up a trustee can prove only against a borrower and guarantors; and main terms of covenants given by borrowing company.

Disclosure for public offers of "prescribed interests" mirrors that required for other securities. Additionally, a trust deed containing covenants regarding the management of the enterprise in which the interests are offered must be registered.

A draft prospectus is submitted to the local CAC for review together with copies of experts' consents, material contracts, consents of trustees, auditors, lawyers, bankers and stockbrokers and a statutory declaration by the solicitor engaged in preparation of the prospectus, verifying the registration copy. The CAC suggests amendments that are incorporated into the draft in the same manner as in the United States. The process takes two to three months, sometimes longer.

Where stock exchange listing is sought, the exchange must receive the documents submitted to the CAC, and the issuer's constituent documents, within one month of announcing the closure of the offer. 14/ Appeal to the courts may be available under the Securities Industry Act of each state if the CAC refuses to register a prospectus. Review is limited to ascertaining whether the NCSC or CAC abused their powers and discretion, and the court will not address the merits of the NCSC or CAC's decision. If an exchange rejects a listing application, the courts similarly may review the matter to ensure that the stock exchange has complied with its contractual duty to give fair and honest consideration to any application, but will not address the merits of the case.

Australia does not have an integrated disclosure system. This, together with the requirement that prospectuses may not be more than six months old, means that issuers involved in repeat or continuous offerings must completely reproduce their prospectuses. In 1984, however, the NCSC approved the use of a

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14/ Off-exchange selling can take place once the prospectus is registered and issued even though listing by the exchange has not yet been granted. If listing is applied for and refused, however, all allotments and issues pursuant to the prospectus are void and money received must be returned.

summary prospectus by seasoned debenture issuers and cash management trusts. A more extensive study of the prospectus provisions is under way to determine whether to recommend an integrated disclosure and shelf registration system such as that currently in operation in the United States.

6. Secondary Market

Although the matter is not free from doubt, secondary offerings seem to be covered by the prospectus requirements to the same extent as primary offerings. Thus the practice has been to register a prospectus whenever securities are offered to the public. This is not necessary, however, for secondary trades made through the stock exchanges.

Continuing disclosure requirements are found in the Companies Code, which requires that an annual return be lodged, together with audited accounts, with the NCSC. This report is presented at the issuer's annual meeting of shareholders within 4-1/2 months of the end of the issuer's fiscal year. 15/ If a corporation has issued debentures to the public, quarterly reports and half-yearly income statements must be filed with the NCSC and the trustee for such debentures.

15/ For prescribed interests, the report must be presented within two months of the end of the financial year. No effort is made to dictate the contents of accounts relating to prescribed interests, which are prepared by the trustee.

Annual reports include, in addition to standard information about the company and its activities, the following audited accounts:

- Balance sheet;
- Profit and loss account;
- Details of consolidated profit or loss;
- Review of operations for year, results of operations;
- Events subsequent to balance date affecting results;
- Details of any securities issued;
- Dividend information on dividends received and distributed;
- Interest paid;
- Provision for bad debts and writing down of assets;
- Charges on assets and contingent liabilities;
- Unusual items in year's accounts;
- Amount of profit or loss arising from sale or revaluation of assets;
- Depreciation;
- Aggregate emoluments of directors and auditors; and
- Provision for income tax.

The AASE requires that listed issuers publish annual reports within four months of the end of the issuer's fiscal year. The issuer's consolidated accounts must also include certain information additional to that required under the Companies Code, the most significant being the annual turnover (gross operating revenue). Non-mining companies must file preliminary annual reports with their home exchanges within three months of year-end and half-yearly reports within three months of the half-year. Mining companies submit quarterly reports with full details of their activities to their home exchanges.

7. Liability

Directors, promoters, or persons who have authorized or caused the issue of a prospectus, are liable to pay compensation to all persons who subscribe for or purchase securities in reliance on the prospectus for any loss or damage sustained by reason of any untrue statement or nondisclosure of material matters in the prospectus. A due diligence defense is available to such persons for untrue statements that were believed to be true, although strict liability apparently attaches to any nondisclosure of material matters. 16/ Common

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16/ Section 107, Companies Code. Very few lawsuits have been brought under this provision. Class actions are not available with respect to such provisions, and contingency fees are illegal. Those actions that are brought tend to be by individuals or by the regulatory authorities.

law tort liability exists but has not been applied in the prospectus context.

Persons authorizing or causing the issue of a prospectus may be guilty of a criminal offense under the Companies Code for untrue statements or nondisclosure unless they can prove immateriality or inadvertence. 17/ Liability may also attach under other legislation such as the Trade Practices Act or the Securities Industry Act. Most state criminal codes also have provisions applicable to securities matters, in particular to the making of false statements with intent to induce investment.

8. Rating System, Withholding Tax, Limitations on Transferability

Established in 1981 in Melbourne, Australian Ratings gained prominence when it correctly predicted the demise of a highly regarded Australian company. The credit agency now rates both domestic commercial paper and corporate bonds.

Withholding taxes of 30 percent are applicable to dividend payments, reduced to 15 percent for residents of countries with which tax treaties are in effect. A ten percent

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17/ Sections 108 and 563(2), Companies Code.

withholding tax is levied on interest payments, although certain exemptions are available.

Foreign funds account for about ten percent of all investment; the United States and United Kingdom are the largest investors. Such foreign investment is subject to approval by the Foreign Investment Review Board ("FIRB"), an advisory body which makes recommendations to the Commonwealth Treasurer, who is responsible for foreign investment policy. Transactions subject to review by the FIRB include acquisitions of the assets of, or substantial interests in, Australian corporations by foreign persons; proposals by foreign persons to establish finance, insurance, media, aviation or uranium businesses; proposals to invest more than A$5 million (currently about US$3.2 million); certain real estate transactions; and direct investments by foreign governments or their agencies. There are no exchange control limitations on transactions by non-residents on the stock exchanges.

H. SWITZERLAND

1. Description of Statutory Scheme and Regulatory Authority

Although federal and cantonal statutes provide some regulation of offerings of securities in Switzerland, most regulation is accomplished by the rules of self-regulatory bodies, such as the stock exchanges and the Swiss Bankers' Association. Swiss stock exchanges are members of the Association of Swiss Stock Exchanges. No federal government agency has been established to regulate the securities markets, although the Swiss National Bank, which is under supervision of the federal government, has some supervisory authority over offerings for economic reasons.

The applicable statutes, rules and agreements are as follows:

1. The Swiss Code of Obligation (the "Code") specifies limited disclosure rules for offerings by domestic issuers.
2. Cantonal laws in Basle and Zürich regulate the stock exchanges in those cantons. In Geneva, the stock exchange has adopted its own rules.
3. The Swiss Federal Law on the National Bank provides that the Federal Council may prohibit or limit

offerings for economic reasons. 1/

4. Article 8 of the Swiss Federal Banking Law provides for advance notice to the National Bank in connection with dealings in foreign securities. The National Bank may forbid or condition these offerings for economic reasons. 2/

1/ If the balanced economic development of the country is disturbed or threatened by an inflow of money from abroad, the Council may, inter alia:

1. limit or prohibit payments of interest abroad;
2. limit foreign exchange transactions by foreigners; and
3. limit or prohibit the acquisition of domestic securities or borrowing by foreigners.

2/ Pursuant to Article 8, banks and financial companies (defined as companies of a banking nature which do not solicit the public for deposits) which intend to conclude, or to participate in, certain transactions must inform the National Bank in advance of:

1. foreign loans, whether as an investment of the bank itself, for issue to the public or taken on commission for placement;
2. the purchase and issuance of shares of foreign companies unless the transaction is made pursuant to exercise of an option for the increase of share capital;
3. credits and investments abroad - whether made by granting a loan for more than 12 months or by purchasing foreign notes or treasury bills for 12 months or longer or for a shorter period where there is an undertaking to allow an extension for more than 12 months; and
4. participation in an initial placement of foreign bonds with a term of 12 months or more.

The National Bank is authorized to forbid or condition these transactions if the trend of exchange rates, interest rates or economic interest of the

(continued . . .)

5. The Swiss Brokerage Convention (adopted by the Association of Swiss Stock Exchanges) fixes minimum brokerage fees.

6. The Convention Governing the Admission of Foreign Securities for Trading and Listing on the Swiss Stock Exchanges adopted by the Association of Swiss Stock Exchanges refers to the Swiss Admissions Office decisions concerning listing of foreign securities on Swiss stock exchanges. Decisions of that office to refuse listing are binding, but a decision to permit listing does not obligate the exchange to list.

7. Agreement XVII of the Swiss Bankers' Association requires that the Cantonal Bank of Bern (acting as coordinating body) be notified of all public offerings by domestic issuers of debt securities in excess of a certain amount.

(. . . continued)
country warrant. The notification requirement is not applicable to transactions and participations therein where, with respect to foreign bonds, it is expected that the amount involved will not exceed SF 3 million (currently about $1.8 million) (or such other amount in excess of this amount as is fixed by the Bank) and with respect to other transactions if the amount involved will not exceed SF 10 million (currently about $6 million).

2. Nature of Securities Markets

The principal exchanges in Switzerland are Geneva, Basle and Zürich. Four other exchanges, Bern, St.-Gall, Neuchatel and Lausanne, conduct more limited trading.

Trading of securities is permitted off the exchanges both prior to and after listing. In fact, a substantial volume of securities is traded over-the-counter even though the securities are listed on the exchanges. Most trading off the exchanges is conducted by banks and financial institutions. Banks often execute trades by transferring securities among their customers' accounts to effectuate customer transactions. Recently, an active, unregulated secondary market has developed among banks and financial institutions for privately placed debt securities.

There is no officially established over-the-counter market or quotation system. The "Vorborse" is an unofficial market for trading prior to official listing on the Zürich Stock Exchange, and the "Ausserborse" is an unofficial market dominated by the Swiss Bank Corporation (one of the largest Swiss banks) and the Volksbank Willisan, Lucerne branch (a regional bank), where shares of a regional character are traded.

Unofficial trading, consisting primarily of telephone calls among banks normally commences on the "Vorborse" two days following the close of the subscription period in an initial public offering. Official trading on the exchange takes place only after all formalities have been completed and physical certificates printed and distributed, often 2 to 3 months following the offering. The Zürich Stock Exchange has issued rules concerning trading and listing on the "Vorborse." In Geneva and Basle, there are no special rules for trading prior to listing.

3. Issuers

Most Swiss companies traded on the exchanges are large, well-known companies. Many Swiss companies remain privately held and raise capital by issuing debt in the public markets. Governmental institutions, including the Swiss Confederation, cantons, municipalities and other public institutions, offer debt securities in public markets and list these securities on the exchanges.

As of the beginning of 1986, there were 315 companies with equity shares listed on the Zürich Stock Exchange. Foreign companies accounted for 184 of this total. Of the listed companies, 19 were newly authorized in 1985 to list their equity on the Zürich Stock Exchange, with 9 of these being foreign issuers. There were new listings in 1985 of bonds and debentures totalling SF 25 billion ($10,196 million), as compared with listings of SF 21 billion ($8,769.4 million) on the Zürich Stock Exchange in 1984. The domestic private sector accounted for SF 9 billion ($3,711.5 million) of the 1985 total, the domestic government for SF 3 billion ($1,177 million) and SF 13 billion ($5,307.5 million) were international issues. 3/

Also as of the beginning of 1986, there were 310 companies with equity shares listed on the Geneva Stock Exchange. Foreign companies accounted for 197 of this total. Of the listed companies, 18 were newly authorized in 1985 to list their equity on the Geneva Stock Exchange, with eight of these being foreign issuers. There were new listings in 1985 of bonds and debentures totalling SF 21 billion ($8,513.7 million), as compared with listings of SF 18.7 billion ($7,959 million) on the Geneva Stock Exchange in 1984. The domestic private sector accounted for SF 7 billion ($2,683.8 million) of the 1985 total, the domestic government for SF 2 billion ($852.9 million) and SF 12 billion ($4,976.9 million) were international issues.

As of the beginning of 1986, there were 291 companies with equity shares listed on the Basle Stock Exchange. Foreign companies accounted for 182 of this total. Of the listed companies, 16 were newly authorized in 1985 to list their equity on the Basle Stock Exchange, with 10 of these being foreign issuers. There were new listings in 1985 of bonds and

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3/ International bonds include Eurobonds and foreign bonds.

debentures totalling SF 23 billion ($9,168.3 million), as compared with listings of SF 17 billion ($6,903.6 million) on the Basle Stock Exchange in 1984. The domestic private sector accounted for SF 8 billion ($3,265.1 million) of the 1985 total, the domestic government for SF 3 billion ($1,177 million) and SF 12 billion ($4,726.2 million) were international issues.

4. Types of Securities Traded

A variety of financing instruments are traded in the Swiss markets. Convertible bonds, floating rate notes, subordinated debentures and warrants have gained acceptance. Bonds issued by foreign borrowers, denominated in Swiss francs, are a significant source of capital in international finance.

Foreign shares are traded on the exchange (a) as registered shares, (b) as shares registered in the name of a Swiss bank, assigned in blank by such bank, or (c) as shares registered in the name of the foreign issuer and held by one of the Swiss banks, with respect to which bearer shares are issued and traded.

Although no specific requirements regarding shares have been adopted by the various stock exchanges, as a general rule each share is required to have one vote. However, certain securities known as dividend-right certificates and participation certificates, which have some of the characteristics of non-voting shares, may be admitted to listing.

5. Primary Offerings

Banks play a vital role in the public distribution of securities in Switzerland. Unlike their counterparts in the United States, Swiss banks actively participate in underwriting offerings, managing investment portfolios and trading in securities. Foreign investment banks and securities dealers also can participate in underwriting syndicates for domestic Swiss offerings. There is no legal requirement that a Swiss bank be among the underwriters.

Firm commitment underwritings are the most common method of distribution in Switzerland. 4/ Syndicates consisting of the largest Swiss banks account for the bulk of the volume of underwritten offerings. "Direct placements," in which the company bears the risk, recently have been utilized more frequently in private placements due to increasing competition in the international markets. However, such placements are unusual in public offerings. Subscription periods generally last five to six days following publication of a prospectus in

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4/ With respect to government bonds, in 1980 the Swiss Government introduced a tender system, with issue prices established as a function of investors' bids. Successful bidders receive the bonds at the same, uniform price.

the newspaper. The most common distribution method consists of sending short subscription forms to customers of the syndicators. The entire distribution process generally takes approximately six weeks.

Shares of a foreign company are generally introduced into the Swiss markets through portfolios of the banks' clients. Actual distribution to the public through the stock exchanges takes place when a certain amount of shares of the foreign company is held by residents in Switzerland and the company has acquired a reputation in Switzerland.

Pursuant to the Code, any offer of newly issued shares to the public must be made by means of a prospectus by which the public is invited to subscribe. 5/ The disclosure required is not extensive. 6/ It includes the latest balance sheet and profit and loss statement with an auditors' report and certain other information.

Bonds may only be submitted for public subscription or introduced on the stock exchange if a prospectus is used. 7/ Prospectus requirements for bonds are similar to those for the

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5/ Art. 650. There is no prospectus requirement under the Code when previously issued shares are offered to the public. With respect to listed companies, however, the exchanges impose such a requirement.

6/ Arts. 631, 651 Code of Obligations.

7/ Section 1156.

issue of new shares. 8/ In addition, the prospectus must contain detailed information concerning the bonds, especially the interest terms, terms of repayment, special security provided for the bonds and any representation of the bond creditors by a community of creditors. 9/

Pursuant to the stock exchange rules of each of the major exchanges, an application for listing must be filed through at least one bank or stock exchange firm which is admitted to the exchange and licensed to trade on the floor of the exchange. Following approval and application for listing, the application must be posted for at least four days on the premises of the exchange. If no objection is made by members of the Association of Swiss Stock Exchanges within this period, the securities may be listed.

Prior to listing, an introductory prospectus must appear in the daily newspaper in one of the three national languages, French, German and Italian. If the application for listing has been preceded by a public offering, the prospectus used in that offering may be used if it is no more than 6 months old. The prospectus must include the necessary information for an

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8/ Sections 1157-1186 of the Code of Obligations.

9/ The Code contains provisions vesting certain powers within a representative who may act on behalf of the creditors of bonds issued to the public by an obligor domiciled or having a business establishment in Switzerland. The provisions do not apply to governmental bonds.

assessment of the securities to be introduced. The issuer must confirm by its signature the correctness of the information contained in the prospectus and the prospectus must contain a request for listing by the sponsoring bank or stock exchange firm.

For issuances by companies that already have securities listed, the board of the stock exchange may waive the requirement of a detailed prospectus and approve admission on the basis of an abbreviated prospectus. 10/

The placement of medium- and long-term government bonds is accomplished through the use of a "tender system." The system provides for the purchase of all offered bonds at a common price which is arrived at through competitive bidding. There are no restrictions regarding who may bid for these securities.

6. Secondary Market

A large amount of secondary market trading is carried out directly among the banks and financial institutions rather than on the exchanges. The banks do not act as market-makers, but may execute transactions either in-house or with another bank

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10/ For issues by governments or municipalities, the prospectus must contain sufficient information concerning the financial status, revenues and expenditures of the public body concerned.

at the current price of the stock exchange where the security is listed.

There are no federal laws specifically restricting or prohibiting foreign persons or entities from engaging in securities transactions on a commercial basis in Switzerland. However, in Zürich and Basle, a cantonal license is required to engage in commercial transactions in securities. Such license will be provided only to an office established in the canton from which the license is requested. Representation and transmission activities of the representatives of foreign brokers located in Geneva are limited to advising and counseling local banks or non-bank financial institutions and transmitting orders given by such entities to an office abroad.

The Uniform Regulations adopted by the three main stock exchanges provide that companies whose securities are listed must publish a printed annual report to be made available to shareholders and bondholders. The bank that requests admission to listing for a company must submit the annual accounts to the appropriate stock exchange and report to the board of the exchange any change in the articles of incorporation of the issuing firm or any information received from the issuing firm which could materially affect the financial position of the company or the listing. All later publications of the company intended for shareholders (such as those relating to dividends) must appear in a daily newspaper in the city where the securities are listed.

7. Liability

Pursuant to Article 752 of the Code, individual stockholders or bondholders may bring action for statements in a prospectus regarding securities of a Swiss company that are incorrect or do not comply with legal requirements against anyone who has cooperated intentionally or negligently in the issuance. It is unclear whether these laws apply to the distribution of securities of foreign issuers. However, lower Swiss courts have imposed liability for foreign issuances where the transaction was expressly subject to Swiss law. In the absence of a specific provision in the Code, general tort liability may be imposed for securities violations.

8. Rating System, Withholding Tax, Limitation on Transferability

A withholding tax of 35 percent is imposed on dividend and interest payments. However, pursuant to a tax treaty with the United States, withholding for United States citizens on Swiss securities is reduced to 5 percent on interest and 15 percent on dividends.

The investment in a real estate company by foreigners is prohibited under a law which prohibits foreigners from purchasing Swiss real estate.

The transfer of registered shares of a Swiss issuer is sometimes restricted by the issuer to Swiss residents. 11/ No statutory provisions restrict transfer to foreigners, however.

11/ Foreign equity ownership has tended to be through bearer shares with reduced voting rights or certificates of participation with no voting rights. A bank in Zürich found a way to circumvent this practice by offering foreigners warrants for equity securities. Several other banks have followed this procedure. The underlying shares are held in blocked accounts at the banks issuing the warrants. Such warrants often trade above the issue price of the securities. They can be traded between foreigners (who thus participate indirectly in the registered share market) but exercised only by Swiss nationals.

I. NETHERLANDS

1. Description of Statutory Scheme and Regulatory Authority

The issuance and trading of securities listed on the Amsterdam Stock Exchange (the "Exchange") are subject to the regulations of the Exchange. The implementation of these regulations is largely carried out by the Amsterdam Stock Exchange Association, a self-regulatory organization.

In addition, the Netherlands recently enacted the "Securities Trading Act" (the "Act"), 1/ to regulate trading in unlisted securities, and the Securities Trading Decree (the "Decree") to implement parts of the Act. The Act, which does not apply to securities listed on the Exchange, prohibits the following activities (except under limited circumstances) in or from the Netherlands:

(1) making a primary offering of securities to individuals not engaged in the business of dealing or investing in securities without making available a prospectus that meets the requirements of the Decree;

(2) acting without a license as an intermediary in securities transactions for individuals or

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1/ October 30, 1985. The Act took effect on May 1, 1986, although its main prohibitions apply as of July 1, 1986.

companies which do not regularly issue securities or engage in the business of investing or trading in securities; and

(3) offering without a license units of participation in a mutual fund to individuals or companies not engaged in the business of dealing or investing in securities.

The Act on the Supervision of the Credit System may apply concurrently with the Act with respect to the public issue of debentures with a denomination of less than DG 100,000 (currently about $44,000) unless (1) the instruments are or will be listed on an exchange (excluding the Parallel Market discussed below) in the European Communities, or (2) the company issuing or dealing in the instruments is registered and subject to supervision by De Nederlandsche Bank NV as a "credit institution."

The Minister of Finance (the "MOF") is charged with granting licenses and exemptions under the Act, and, pursuant to the Stock Exchange Law of 1914, supervises the Exchange. The Stock Exchange Listing Decree of 1983 (the "1983 Decree") implements certain of the EEC directives and distributes the powers of the competent authority, within the meaning of the directives, between the MOF and the Exchange. 2/ The 1983 Decree provides that any amendment to the Exchange Listing Manual must be presented to the MOF for prior approval.

2. Nature of Securities Markets

The Exchange is the only securities exchange in the Netherlands, although the Amsterdam Parallel Market (the "Parallel Market") exists as part of the Exchange, with less stringent listing requirements. The European Options Exchange and a gold futures market are also located in Amsterdam. Both domestic and foreign companies may be listed on the Exchange and on the Parallel Market.

3. Issuers

As of the beginning of 1986, there were 474 companies with equity shares listed on the Exchange. Foreign companies accounted for 242 of this total. There were new listings in 1985 of bonds and debentures totalling DG 42 billion ($12,694.4 million), as compared with listings of DG 31 billion ($9,743.9 million) on the Exchange in 1984. The domestic private sector accounted for DG 11 billion ($3,276.3 million) of the 1985 total, the domestic government for DG 27 billion ($8,026.8

2/ *See* discussion in part IV.A., *supra.*

million), and DG 4 billion ($1,355.3 million) were international issues. 3/

4. Types of Securities Traded

Securities traded on the Exchange are usually in bearer form. If the securities are in registered form they are often deposited with a depositary and the depositary receipts are traded in bearer form. Both corporate and government bonds are exchange listed, as are shares of investment companies and funds. Eurobonds are traded but not officially quoted.

5. Primary Offerings

a. Participants in a Distribution

The major banks play a primary role in the distribution process, acting both as investment banks and securities brokers. There are also companies other than banks that specialize in the securities industry. For an offering solely in the Netherlands, a major bank is generally selected for placement of the issue. The bank may syndicate the issue with other banks or securities firms. Although no law prohibits

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3/ International bonds include Eurobonds and foreign bonds.

foreign participation in underwritings, as a matter of practice, foreign firms do not act as lead managers of guilder-denominated bond issues in the Netherlands unless Dutch banks are afforded comparable treatment in the parent country of the foreign firm.

Offerings may be made on a firm commitment or a best efforts basis. The listing manual of the Exchange provides that, in the case of an underwritten issue of debentures for a principal amount of DG 150 million (currently about $66 million) or more, all banks and securities brokers who are members of the Exchange and who qualify must be invited to act as major underwriters or minor underwriters. This group must be allowed as a whole to participate in up to 25 percent of the issue. In the case of a multinational offering, this requirement might not be imposed, provided allotments are made among members of the Exchange on a systematic basis.

Securities issued by the government of the Netherlands are marketed by the MOF, which offers the securities for auction to members of the Exchange. No other public authorities or institutions in the Netherlands issue securities but rather finance capital improvements through private placements or issues floated by the Bank Voor Nederlandsche Geemeenten (Bank for Dutch Municipalities) or the Nederlandse Water Schap Bank (Bank for Dutch Waterboards) on the Exchange. The offerings of the Bank for Dutch Municipalities are marketed by a group of

Exchange members, while the offerings of the Bank for Dutch Waterboards are underwritten by a syndicate of Dutch banks.

b. Disclosure Requirements

The Act permits the sale (other than within a limited group) in or from the Netherlands only of securities that are or will be officially listed on an exchange (as defined in the Act), of unlisted securities offered with a generally available prospectus that meets the requirements of the Decree and to which every written announcement of the offer refers, and securities for which an exemption applies or a dispensation from the MOF has been granted. The prospectus requirements are based on the regulations of the Exchange and closely resemble the listing directives of the EEC.

An "exchange" is deemed to include any securities exchange in the Netherlands or in one of the of the Member States of the European Communities or an exchange designated as such by the MOF. The Swiss exchanges of Basle, Bern, Geneva, Lausanne and Zürich and the United States stock and futures exchanges subject to the supervision of the Securities and Exchange Commission (including NASDAQ) or of the Commodities Futures Trading Commission have been so designated by Ministerial Decree. The Parallel Market is also considered an exchange.

The requirement for a prospectus with respect to securities that are not listed or for which an exemption or dispensation is unavailable also applies to secondary offerings of securities, defined as including those that have only been available to a limited group since issuance. A limited group has been interpreted as a group that is of limited size and clearly defined, where there is more than just a financial relationship between the group and the party offering the securities and the offer is open for acceptance only by the members of the group.

The Decree sets forth the prospectus requirements for unlisted securities. The requirements depend on the type of securities being offered. Every prospectus for unlisted securities must contain a statement from an "expert" 4/ that the prospectus contains the information required pursuant to the provisions of the Decree.

The prospectus contains information regarding the securities, the persons responsible for the content of the prospectus, including the experts, and the issuing institution. The prospectus also describes the issuer's capital, activities, management and prospects, and includes balance sheets and profit and loss accounts and statements of source and

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4/ An "expert" is a registered accountant or a person to whom a license has been granted by the Minister of Economic Affairs as a certified accountant (an administrative consultant registered pursuant to the Certified Accountants - Administrative Consultants Act) and includes persons admitted as accountants by a revocable license from the Minister of Economic Affairs on the basis of a certificate of professional proficiency obtained abroad.

application of funds for the last three financial years, which must be audited. The latest financials must be no more than 18 months old at the time the prospectus is made available. If more than nine months have expired since the end of the last financial year, unaudited interim figures for the first six months must be included with the prospectus.

A prospectus is also provided with respect to government securities, but it generally contains more limited information than that required by private issuers.

c. Listing Procedures

The Exchange imposes requirements as to the minimum volume of a placement and, in the case of listed securities, the minimum portion thereof to be available for subscription by the public. The Exchange also requires that a prospectus be available as a precondition to listing; however, an exception may be granted in the case of an offering of an additional portion of the securities of a listed company not exceeding 10 percent of the number or corresponding value of securities of the same category that have already been admitted to listing. Such an exception will only be granted if sufficient particulars have been announced regarding the number and kind of securities to be admitted and the terms and conditions of the issue.

The Exchange reviews the prospectus or information submitted pursuant to an exception from the prospectus requirement, and must give its approval prior to publication.

In the case of an underwritten offering, the sponsoring bank advertises in the "Bulletin" of the Exchange that on the next business day copies of the prospectus will be available at the offices of the Exchange and of the sponsoring bank. On the day on which the prospectus first becomes available, an application for admission to official listing must be filed with the Exchange. The application must be signed by the issuer and the sponsoring bank.

The MOF admits securities to official listing, but has delegated to the Exchange the power to admit securities provisionally subject to admission by the Minister. The Exchange has the power to suspend a listing and to delist securities.

A prospectus is required for subsequent offerings by listed companies, but may be waived by the Exchange.

6. Secondary Market

The Exchange requires companies listed either on the Exchange or Parallel Market as a part of their continuing disclosure obligations to, inter alia, make available to the public, as soon as possible and within a period established by the listing agreement, annual accounts, an annual report and a half yearly report, and to inform the public of any changes in information stated that may affect shareholder rights or facts or occurrences that may have a substantial influence on the price of the securities.

In the case of a non-Netherlands issuer, the information may be in English. The information must be made available either by advertisement or in some printed form available in a manner indicated by advertisement. In addition, the issuer must publish information on dividends.

7. Liability

Breach of provisions of the Act constitutes a criminal offense under the Economic Offences Act and may result in a penalty of six months imprisonment and/or a fine of DG 10,000 (currently about $4,500) or DG 25,000 (currently about $11,000) in case of aggravating circumstances. The Penal Code also contains provisions which may apply in the case of fraudulent conduct in connection with securities transactions.

8. Rating System, Withholding Tax, Limitation on Transferability

There are no Dutch rating agencies.

Dividends must be payable in Amsterdam and an issuer of listed securities must appoint a paying agent in Amsterdam.

Dividends are subject to a 15 percent withholding tax. Interest on bonds is paid without withholding tax.

There are no restrictions on the purchase or sale of securities on the Exchange. Profits and revenues may be repatriated at will.

V. TENDER OFFERS

A. INTRODUCTION

The tender offer, which has been an important technique for acquisition of publicly-held corporations in the United States for a number of years, is becoming an increasingly important technique in the foreign and international markets as well. The principal advantage of the tender offer is that, unlike other forms of acquisition, approval by the board of directors of the subject company is not required. In the last decade, an increasing number of foreign bidders have utilized tender offers to acquire United States corporations, often on a hostile basis. For example, in fiscal 1986, 21 tender offers subject to the Commission's rules were filed by foreign bidders for the securities of domestic corporations. Seven of those offers were not approved by the target's board of directors.

By commencing a bid for a domestic corporation, foreign companies subject themselves to the same federal and state regulatory requirements that apply uniformly to foreign and domestic bidders. Even where the foreign bidder is seeking control of another foreign corporation, United States law governing tender offers may apply if the offer is made to shareholders residing in the United States. Compliance with United States tender offer regulation, however, may pose compliance issues for foreign bidders. In addition, foreign bidders may face regulatory requirements that restrict the ability of foreign investors to participate in certain industries.

With the internationalization of the securities markets, tender offer bids to acquire control of corporations with shareholders residing worldwide must comply with the regulatory requirements of a number of countries and political subdivisions. This is a particularly significant concern with respect to exchange offers, where the securities offered by the bidder in exchange for the target's securities must comply with the registration and distribution requirements in each country where the securities are offered.

The following sections provide a summary of the basic regulatory requirements with respect to tender offers of the United States and eight other countries. The special regulatory requirements and problems facing foreign bidders when making a tender offer in the United States are also examined.

B. COMPARATIVE STUDY OF TENDER OFFER REGULATION

UNITED STATES

1. Regulation

Tender offers for the securities of companies reporting under the Securities Exchange Act of 1934 are regulated by the

Securities and Exchange Commission ("Commission") under the Williams Act provisions of the Act. Additionally, exchange offers are subject to registration under the Securities Act of 1933. The majority of states have also passed takeover statutes. The New York Stock Exchange also has rules relating to takeovers, but for the most part these rules are less stringent than the Commission rules. Section 13(d) of the 1934 Act imposes reporting requirements for substantial acquisitions of equity securities. Section 13(e) relates to tender offers by an issuer for its own securities. Section 14(d) requires any person making a tender offer for another company's securities to file information with the Commission and disseminate it to shareholders, as well as comply with certain procedural safeguards. Section 14(e) is an antifraud provision relating to tender offers.

The term "tender offer" is not defined, necessitating interpretation on a case-by-case basis by the courts. The dividing line between pre-offer acquisitions subject to Section 13(d) and tender offers subject to Section 14(d) is unclear.

2. Procedures

The federal securities laws do not require that persons acquiring over a certain percentage of another company's securities commence a tender offer. The 1934 Act requires only that any person acquiring the beneficial ownership of more than five percent of a class of equity security registered under the 1934 Act must disclose such holdings, and all material changes therein, on a Schedule 13D or 13G filed with the Commission within 10 days of the acquisition. Information concerning the person acquiring the securities, including his citizenship, as well as the person's plans and proposals with respect to the subject company must be disclosed.

Concurrently with making a tender offer that would result in ownership of more than five percent of a class of registered equity security, the person or group making the offer must file a Schedule 14D-1 with the Commission. The Schedule 14D-1 must also be delivered to the target company, any other bidder having filed a Schedule 14D-1 relating to the same class of securities, and each national securities exchange upon which the target class of securities are listed. The staff of the Commission will normally review and comment on the disclosures shortly after the filing of the Schedule 14D-1.

Substantially all the information required by Schedule 14D-1 must also be disseminated to the target shareholders. This may be done by long form publication (i.e., publishing all information in a newspaper advertisement); by summary advertisement with full tender offer material being furnished to shareholders requesting such material; or by mailing the materials to the subject company's shareholders. The subject company must on request either provide the offeror with its shareholder list or distribute the materials itself.

Within 10 days of dissemination of the offer, the subject company must disseminate to its shareholders a statement disclosing whether it recommends acceptance, recommends rejection, is taking a neutral position or is unable to take a position. The reasons for the target's stance, including its inability to take a position, must be stated. Other information as set forth on Schedule 14D-9 (see below) must be disseminated to the shareholders. The Schedule 14D-9 is also reviewed and commented upon by the Commission's staff. Simultaneous with distribution to shareholders, the subject company must file the Schedule 14D-9 with the Commission, and deliver copies to the offeror and each exchange upon which the target securities are listed. Third parties making solicitations or recommendations must also deliver copies of Schedule 14D-9 to the SEC, exchanges, the offeror and the subject company.

Issuers making a tender offer for their own securities must file a Schedule 13E-4 with the Commission. Purchases by a target during a third party tender offer are also subject to disclosure requirements under Rule 13e-1. If the purchases by an issuer or an affiliate of the issuer result in the securities no longer being publicly traded, compliance with the disclosure requirements of the Commission's "going-private" rule, Rule 13e-3, which is designed to elicit disclosure relating to the fairness of the transaction, will be required.

3. Disclosure

Disclosure under Schedule 14D-1 covers the following matters:

- Information about the offer, including expiration date, offering price, withdrawal rights, proration;
- Trading history of the subject security;
- Information about the offeror and its officers, directors, partners, and controlling persons, including employment histories and involvement in violations of securities laws;
- Past contracts, transactions, or negotiations with target;
- Source and amount of funds or other consideration used in offer;
- Purpose of offer and plans of offeror after acquiring securities to effect extraordinary corporate transactions;
- Holdings of offeror and its principals in subject company; transactions in subject company's securities in the last 60 days;
- Terms of any contracts, understandings, or relationships with respect to target's securities;
- Persons offeror has retained to assist in offer; and

- In the case of an exchange offer, financial information about the offeror.

The information to be disclosed on Schedule 14D-9 covers the following matters:

- Any conflicts of interest between filing person or affiliates and (a) the subject company, its affiliates, officers and directors, or (b) the offeror, its affiliates, officers and directors;
- Nature of and reasons for solicitation or recommendation;
- Identity of any person retained in connection with the solicitation or recommendation;
- Transactions in subject class of security effected by filing persons, officers, affiliates or subsidiaries in last 60 days or intentions of such persons to sell or hold such securities; and
- Any negotiations or transactions being conducted in response to the tender offer that would result in (a) extraordinary corporate transactions such as merger or reorganization involving the subject company or any subsidiaries, (b) purchase, sale or transfer by the target of material assets by the target or subsidiaries, (c) tender offer for, or acquisition of, target's own or another's

securities, or (d) any material change in target's capitalization or dividend policy.

4. Substantive Protections

Offering Period: Commission rules require that a tender offer be open for a minimum of 20 business days from the time it commences. There is no specified time by which it must be completed. The offer must extend at least 10 days beyond any announcement of a change in tender price or change in the number of securities to be acquired. Any other material change in the terms or conditions of the offer will likewise require the bidder to extend the offer.

All-holders: Tender offers must be made to all holders of the class of securities subject to the offer, unless prohibited by a state statute from making offers in that state.

Best Price: The consideration paid to any shareholder pursuant to an offer must be the highest consideration paid to any other shareholder during that offer.

Withdrawal Rights: Commission rules provide that any person who has deposited securities pursuant to a tender offer has the right to withdraw any such securities during the period such offer remains open. Tendered securities that have not been accepted for payment may be withdrawn after 60 days following commencement of the offer.

Proration: Partial offers are permitted, and proration is required.

Antifraud Provisions: In addition to the general antifraud provisions of Rule 10b-5, Rule 10b-13 prohibits purchases of subject company securities by the bidder otherwise than pursuant to the tender offer; Rule 10b-6 regulates purchases by the bidder of the securities it offers in an exchange offer; and Rule 10b-4 prohibits short tendering in connection with any tender offer.

Section 14(e) prohibits fraudulent, deceptive or manipulative acts in connection with a tender offer and gives the Commission authority to define and prescribe means to prevent such fraudulent practices. Pursuant to this authority, the Commission established a "disclose or abstain from trading" rule. Rule 14e-3 prohibits communicating or trading while in possession of certain material nonpublic information, if any person has taken substantial steps toward commencing a tender offer.

UNITED KINGDOM

1. Regulation

In practice, the control of tender offers is exercised by the Panel on Takeovers and Mergers, a self-regulatory body sponsored by the Bank of England and the institutions using the London securities market (the "Panel"). 1/ The Panel works closely with the Stock Exchange, and both the Stock Exchange and the Panel require disclosures to be made in takeovers. The Panel's requirements are set out in the City Code on Takeovers and Mergers (the "City Code"), which sets out general principles for the regulation of tender offers. The City Code applies to public and certain private companies, while Stock Exchange disclosure requirements apply only to listed companies.

1/ The Department of Trade and Industry ("DTI") exercises authority over fraudulent or misleading statements made in circulars relating to takeovers and may regulate the contents of such documents issued by parties licensed by the DTI. The DTI and other government bodies also have the power (never yet used) to prohibit foreign acquisitions in strategic industries. Additionally, the Financial Services Act 1986 sets out the circumstances in which persons holding 10% or less of the shares of a company may require or be required to have their shares compulsorily purchased. Other than these provisions, takeover activity is basically self-regulated.

Additional requirements relating to the acquisition of shares are imposed by the Rules on the Substantial Acquisition of Shares ("SAR"), which are promulgated by the Council for the Securities Industry, a self-regulating organization. The SAR is not concerned only with takeovers. The SAR regulates the purchase of shares representing five percent or more of the voting rights of a company where such an acquisition, when added to the acquiror's existing holding, would represent more than 15 percent of the target's voting rights.

Neither the Code nor the SAR have legal force, but in practice they are the universally recognized market controls in this area. The Code has been referred to in court proceedings, where it has been used as a guide to good commercial practice. Non-compliance with the Code's provisions will likely lead to consequences such as loss of licenses to trade on the Stock Exchange.

In addition to setting standards for disclosure and procedure in takeover situations, the Code provides that where any single acquiror acquires more than 29.9 percent of the issued voting capital of a company, it must make an offer for the remaining shares.

2. Procedure and Filing

When a company is notified of a person's serious intention to make an offer, that target company must issue a press notice immediately, followed by a circular to its shareholders and to the Panel. Within one month the offeror must distribute an offer document to target shareholders. This document is subject to the general principle articulated in the Code that such documents must be prepared with the same care as if they were prospectuses. In the case of a listed target company, the offer document is reviewed by the Stock Exchange prior to dissemination. If the target shares are not listed, the offer document need not be reviewed provided that it is being sent to shareholders by a licensed or exempted dealer. Where this is not the case, DTI review and approval must be obtained. Copies must be delivered to the City Panel upon dissemination to shareholders. The Panel, which may be consulted prior to distribution of the offer document on points of difficulty, sometimes requires additional disclosure to be made by supplementary circulars.

In the case of an exchange offer, where the securities offered are to be listed, "Listing Particulars" complying with the disclosure requirements of the Stock Exchange must be distributed together with the offering circular. These give full details of the securities offered as consideration.

The Code provides that the target company's board of directors should advise shareholders of its views on the offer as soon as practicable within publication of the offer document and normally within 14 days.

Offers may be made subject to certain conditions. Offers are usually conditional upon acceptances being received for at least 90 percent of the voting capital and the Code provides that offers must normally be conditional upon acquisition of at least 50 percent. Specific and objective conditions outside the offeror's control may also be attached.

During the course of a tender offer, under a recently amended rule, all beneficial holders of one percent of the target's and offeror's shares must report changes in their holdings on a daily basis.

3. Disclosure

The Code requires that an offeror give details of the following (some of which requirements are incorporated by reference from the Stock Exchange's rules) in its offer document:

- Date of offer, precise terms, how to tender securities;
- Names of offeror and offeror's directors;
- Offeror's intentions regarding the continuation of target's business;
- Intentions regarding any major changes to be introduced in target's business; any redeployment of target's fixed assets;

- Long term commercial justification for proposed offer;
- Intentions as to employment and pension rights of target's employees;
- Holdings of shares in target by offeror and its associates; recent price history of target securities;
- Dealings with target by offeror and its associates;
- Details of agreements with target directors; proposed compensation for loss of office;
- Target shareholders' rights;
- Where the offer is for cash, a confirmation by a third party that sufficient funds are available;
- Where the offer could result in a holding by the offeror of at least 50 percent but less than 100 percent of the target, a statement must be included to the effect that a successful bid may involve transfer of control of the company without the offeror being required to make an offer for the minority shareholding;
- In exchange offers, holdings of offeror's directors in offeror's securities; how directors will be affected by transaction;
- Financial information about offeror:
    - (a) five years' financial statements;
    - (b) latest published audited balance sheet;

(c) material changes in offeror's position since last audited report;

(d) any preliminary or interim financial information released; and

(e) significant accounting policies, important points from notes;

- For listed companies only: Details of both offeror and target's turnover, net profit before tax and rate of dividends for last five years;
- Offeror's business, financial and trading prospects;
- Disclosure of ultimate owner of shares;
- Wording advising shareholders to seek professional advice on the offer; and
- In exchange offer, next dividend or interest payment in which new securities will participate, effect of acceptance of offer on offeror's assets, rights of such securities.

The target company's board of directors' circular must cover the following matters:

- Board's view on offeror's plans for company and employees;
- Target's holdings in offeror, directors' holdings in offeror, independent adviser's holdings in

offeror, directors' intentions as to acceptance of the offer regarding their own shares;

- Directors' service contracts, recent changes therein; and
- Arrangements with regard to dealings in target securities.

The Code also requires that the target board obtain competent independent advice on the offer and make the substance of such advice available to the shareholders.

4. Substantive Protection

Minimum Offering Period: Any offer to the public must remain open for at least 21 days and if it has become unconditional, it must remain open for a further 14 days unless the offeror has stated that no extension beyond the closing day will be made.

All-holders: Equal treatment of all shareholders of the same class is required under the Code.

Best Price: If, while the offer is open, the offeror or any person acting in concert with it purchases shares at a price above the offer price, it must increase its offer price to such higher price, and make an immediate announcement to that effect.

Withdrawal Rights: During the first 42 days after the dissemination of an offer document, no accepting shareholder may withdraw unless the offer has lapsed, or the offeror has failed to comply with certain obligations under the Code. If the offer has not become unconditional as to acceptances after 42 days, then shareholders may withdraw for any reason.

Proration: The City Panel's consent is required for partial offers, which are infrequently made. The Panel may require that partial bids seek statutory control (over 50 percent). Proration is required in the case of partial offers.

Regulation of Purchases Outside the Offer: Unrestricted purchases on the exchange may be made until the 30 percent threshold is met. During an offer for all shares, purchases may be made on the Stock Exchange, although the price paid may affect the offer price. No such purchases are permitted during a partial offer.

Shareholder Approval: Offers that would result in acquisition of over 30 percent of the voting rights, must be approved by a majority of the shareholders; approval is manifested by checking a box on the acceptance form.

JAPAN

1. Regulation

Takeover activity in Japan is regulated by the Securities Bureau of the Finance Ministry ("MOF"). Regulation of tender offers did not exist at all until 1971, when the Securities and Exchange Law of 1948 was amended by the MOF Registration Ordinance Concerning Takeovers, No. 38 of June 9, 1971. Conditions and methods of buying are prescribed by MOF Cabinet Order No. 321 of September 30, 1965 (Amended 1971). Takeovers are rare in Japan, and the introduction of this law represented an attempt to create a structure to deal with anticipated developments in the securities market.

As in the United States, tender offers are not the only means of acquiring large interests in companies. Open market purchases and negotiated transactions may occur without triggering a requirement that a buyer make a tender offer. A tender offer is defined as a public offer to buy, outside the securities markets, shares and other equity-related securities issued by public companies. Tender offers resulting in less than ten percent of the target company's shares being owned by the offeror are not subject to regulation.

2. Procedure and Filings

A tender offer statement containing specified disclosures and other documents relating to the offeror and the terms of the offer is required to be filed in preliminary form with the Finance Minister ten days before it becomes effective. The MOF reviews the documents for adequacy of disclosure. Foreign offerors must use a securities company or bank as their agent in such filings. The offeror must also file a certificate as to the existence of the necessary funds. Prior to the effective date, the offeror sends a copy of the tender offer statement to the target company. After the effective date, a copy must be sent to the stock exchange where the target securities are listed, and a notice of the tender offer must be published in two or more newspapers. The MOF regulates the contents of the public notice.

The offeror must make the offer through a securities corporation. No purchases may be made until the shareholders receive explanatory materials containing the same information as the tender offer statement filed with the MOF and generally similar to the prospectus that would be used in a public offering.

The target company is not required to provide a recommendation to shareholders, but if one is issued, it must be filed in advance with the MOF.

Only two conditions may be imposed on the offer. The offeror may require that a minimum of 45 percent of the target's shares be tendered. Additionally, the offeror may qualify its offer with a provision for possible withdrawal in the event of a change in the target's business circumstances that would seriously undermine the offeror's reasons for making the offer.

Unregulated tender offers (i.e., those for less than ten percent of the target's shares) are subject to prior approval by the securities exchange if the target securities are listed, or the Securities Dealers Association if unlisted.

Japan imposes restrictions on acquisitions of more than ten percent of certain shares of Japanese issuers by foreigners. A report must be made regarding the proposed acquisition, through the Bank of Japan, to the MOF and the minister in charge of the target's industry. A waiting period is prescribed before consummation of the deal.

3. Disclosure

The tender offer registration statement is prepared following the format of Form 1 and covers the following matters:

- Purpose of the offer;
- Duration of offer;

- Number of shares to be purchased, existence of any withdrawal rights;
- Price;
- Source and amount of funds;
- Description of offeror and its affiliates; and
- Offeror's and affiliates' holdings in target company's shares.

If the target company makes a recommendation with respect to a tender offer, its communication must include the following information:

- Grounds for its recommendation;
- Details of discussions at board meeting regarding any recommendation;
- Number of shares in target held by management; and
- Any benefits promised to target management by offeror.

4. Substantive Protection

Minimum Offering Period: A buying period of 20 to 30 days from the date of public offer is mandated.

All-Holders: All shareholders must be treated equally.

Best Price: The offer price may not be decreased, and if increased must be received by all tendering shareholders.

<u>Withdrawal Rights</u>: Shareholders may withdraw freely from agreements to sell target shares during the first ten days following the initial public notice of the offer or the announcement of an alteration to the offer.

<u>Proration</u>: Partial offers are permitted and proration required.

<u>Regulation of Purchases Outside the Offer</u>: In general, purchases in the market are prohibited during a tender offer.

CANADA

1. Regulation

As with other aspects of securities regulation in Canada, the conduct of tender offers is regulated at both the federal and the provincial levels. Where the target is a corporation incorporated under the Canada Business Corporations Act ("CBCA"), the provisions of CBCA apply to takeover bids for such corporation's securities. The CBCA is administered by a government-appointed director (the "Director"). Other federal statutes may also apply. At the provincial level, the provisions of the companies legislation under which a target is incorporated may relate to takeovers, and the Securities Commissions of Alberta, British Columbia, Manitoba, Ontario, Quebec and Saskatchewan all regulate takeovers where holders of target securities reside in those states. The other provincial jurisdictions do not regulate takeovers. A tender offer may thus have to comply with several sets of regulations.

Among the provinces, Ontario has traditionally taken the lead in securities regulation, and its takeover legislation, as embodied in the Ontario Securities Act, has been accepted as a model by the other provinces that regulate takeovers.

The CBCA provides that a takeover takes place once a 10 percent threshold has been met with reference to the securities of a corporation incorporated under its provisions. The

Ontario Securities Act provides that a takeover bid is in progress when a 20 percent acquisition threshold is met. Most other provinces also use the 20 percent threshold figure. In each case when a person purchases or offers to purchase a number of securities that, when added to such person's other holdings, equals the threshold percentage of similar voting securities, that person must comply with the code of conduct set forth in the applicable statutes.

Most applicable Canadian statutes exempt certain acquisitions from the statutory code of conduct. These may include takeover bids made through the facilities of and in accordance with the rules of a stock exchange, takeovers by private agreement with a limited number of security holders, "creeping acquisitions" and transfer of control blocks. The stock exchanges themselves prescribe the manner in which the first category of exempt acquisitions may be made.

It should be noted that Ontario provides that "follow-up" offers must be made where securities are acquired at a premium in transactions exempt from the statutory code of conduct. In such cases the offeror must make an offer of at least the premium price to all holders of the same class of the securities that were acquired in the exempt transaction.

2. Procedure

As in the United States, several Canadian provinces (including Ontario) impose reporting requirements upon persons acquiring significant holdings in companies' voting securities. Acquisitions made prior to the triggering of a tender offer are thus reportable.

Once the threshold requirement has been met, Ontario requires that each target shareholder be provided with a copy of takeover bid circular comprising certain prescribed disclosure (see below). This is not subject to any review. Within 10 days of the date of the offer, the target board of directors must send a directors' circular to each target shareholder. This is also subject to no review.

A similar procedure is in effect in Quebec, but there the documents produced by both the offeror and the target board must be filed with the Quebec Securities Commission ("QSC") upon the day of distribution. The QSC may require further disclosure.

Some provincial jurisdictions only require the use of a directors' circular where the directors of the target company are making a recommendation as to acceptance or rejections.

The CBCA also requires the distribution of a takeover bid circular in prescribed form. This circular must be sent concurrently to each target shareholder resident in Canada, each target director and filed with the Director. The target directors must also distribute a circular. They need not distribute it until at least seven days before the bid terminates or before the sixtieth day of the offering period, whichever is earlier. If it is not distributed within ten days of the offeror's circular, the directors must notify target shareholders that a directors' circular will be forthcoming and may recommend that they do not tender their shares until they receive the directors' circular. The directors' circular must be sent to the target directors themselves, to each target shareholder resident in Canada, to the offeror and to its directors. A directors' circular must be sent whether or not the directors make any recommendation as to the offer.

The only conditions upon which an offer may be made under Ontario law are that a minimum number of shares must be tendered, that undisclosed actions prior to the date of the offer shall not result in material change to the affairs of the company, and that any necessary regulatory approvals be obtained.

3. Disclosure

Disclosure required by Ontario in takeover bid circulars is set out in Form 31 under the Ontario Securities Act. The contents of Quebec's Schedule XI are almost identical and the CBCA disclosure requirements are substantially similar. Form 31 requires disclosure of:

- Holdings and recent trading in target's securities by offeror, associates, directors, and principal shareholders;
- Terms and conditions of bid, method and time of payment;
- Statement that right to withdraw deposited securities exists for 10 days from date of offer;
- Recent volume of trading in target securities;
- Holdings of directors, officers, etc. in offeror;
- Details of any arrangements or agreements between offeror and target officers and directors, including compensation for loss of office;
- Interests of target officers and directors in material contracts of the offeror;
- Details of trading in target's shares by target officers and directors, target itself. The CBCA requires details of all recent trading in target securities;
- Material changes in target's business since last published financials. The CBCA requires distribution of latest published financials in the directors' circular; and
- If approval or rejection of offer is being considered by board, such may be stated and a recommendation made that shareholders' decisions

be deferred until the board reaches a decision.

The CBCA requires details of directors' and officers' service contracts and recent changes therein, and also that the reasons for any recommendation or failure to make a recommendation be given.

In certain circumstances circulars relating to individual directors or officers may be distributed.

4. Substantive Protection

Minimum Offering Period: Ontario requires an offering period of at least 21 days. In the case of partial offers, the offering period may not exceed 45 days. The CBCA provides for similar time periods.

All-Holders Rule: Ontario requires tender offers to be made to all holders of the class of securities sought and all holders of any securities convertible into the securities sought, at the same consideration.

Best Price: Under Ontario law, if during the course of the offer the offeror pays a higher price than the offered consideration for any securities covered by the offer, the offer price is deemed increased. The CBCA contains similar provisions relating to securities tendered pursuant to the offer or purchased outside the offer.

Withdrawal Rights: The Ontario Securities Act permits shareholders to withdraw securities deposited for a period of ten days from the date the offer is made. The CBCA permits target shareholders to withdraw their shares within ten days after the bid is made in all cases, and, in the case of bids for all target securities, at any time after 60 days after the date of the bid, if not taken up by the offeror.

Proration: Both Ontario law and the CBCA permit partial offers and require proration.

Regulation of Purchases Outside Offer: Ontario permits purchases to be made on securities exchanges outside the offer. The CBCA also permits such purchases, but the offeror's intent to make them must be stated in the takeover bid circular.

FEDERAL REPUBLIC OF GERMANY

No formal procedural rules regulating takeover bids exist. Takeovers may, however, be subject to regulation under antimonopoly legislation and the government may restrict the acquisition of shares in companies in certain sensitive industries.

In 1979, the Stock Exchange Committee of Experts, affiliated with the Ministry of Finance, promulgated a set of guidelines relating to takeover bids, entitled "Guidelines for Public, Voluntary Purchase and Conversion Offers and/or Indications to Make Such Offers for Officially Quoted or Semi-Officially Quoted Shares or Transfer Rights" (the "Guidelines"). The Guidelines are not binding and do not give rise to any sanction if breached.

The Guidelines' objectives are equal treatment of all shareholders and adequate disclosure, and they apply to both the offeror and the target.

The Guidelines require that the target of a takeover bid and the stock exchange on which its shares are listed be notified of the bid, and the target's statement be requested.

Immediately thereafter the offeror should publish the offer. The Guidelines state that the offer should contain the following information:

- Name of offeror;

- Class (and maximum number) of shares covered by offer, price offered, how price reached;
- Objectives of offer;
- Offeror's holdings of target's securities, and target's in offeror's securities;
- Statement of target company, if available;
- How offer can be accepted;
- Term of offer;
- Circumstances in which offeror can withdraw;
- Indication that shareholder has right to withdraw;
- Date of payment, tax information; and
- Undertaking by offeror to pay compensation to persons accepting offer if it makes a higher purchase offer in next 18 months.

The Guidelines recommend an offering period of 21 to 60 days, with extension of time in the event changes are made to the terms of the offering. Material facts should be publicized immediately. The offeror should not conclude any transactions in the target shares outside the offer, and in the case of an exchange offer should refrain from actions affecting the value of its own shares. Partial offers should be prorated.

FRANCE

1. Regulation

France has formally regulated tender offers only since 1970, when the Chambre Syndicale (the governing body of the stockbrokers' association) drew up rules regarding takeovers and the Commission des Operations de Bourse (the "COB" -- the government agency regulating the securities markets) adopted a code of practice for all public offers. 2/

Regulation of takeovers is exercised principally by these two bodies, but in certain circumstances two other bodies may be involved. The Finance Ministry has power to regulate foreign investment in France and the Committee for the Supervision of Takeover Bids, formed in 1978, may also make decisions on takeovers referred to it by its members.

The transactions to which tender offer regulation applies -- "public offers to purchase" and "public offers to exchange" -- are not specifically defined. Jurisdiction is also exercised over the transfer of "controlling interests", "control" being decided on a case-by-case basis. Gradual

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2/ The sources of tender offer regulation are the General Decisions of the COB concerning Public Offers (January 13, 1970, amended July 25, 1978) and a General Regulation of the Chambre Syndicale (August 8, 1973, amended August 7, 1978).

acquisitions do not appear to implicate the regulation of acquisitions of controlling interest.

2. Procedure and Filings

Two alternative procedures exist in a takeover. The offeror may purchase a "controlling interest" and follow up that purchase with a public offer to the target's shareholders, or it may make a takeover bid.

In the first instance, the offeror applies to the Chambre Syndicale, which determines whether the initial purchase is of a controlling interest. In the case that it is, the Chambre Syndicale will permit the initial purchase to be made if the offeror undertakes to purchase all the shares offered on the stock exchange over a period of 15 trading days. The Chambre Syndicale publishes a notice in the official stock exchange bulletin, giving the names of offeror and target, and the date, price and number of securities of the initial purchase. The term and price of the offer is also given. Apart from the initial application to the Chambre Syndicale, no filings are made.

A takeover bid is made by offer to all shareholders. The offeror must submit a "note d'information", or prospectus, for COB review and approval. A file regarding the offer is also submitted to the Chambre Syndicale by the financial institution guaranteeing financing for the offer. The Chambre Syndicale pays close attention to the price offered, and the financial institution's justification of such price. When the Chambre Syndicale is satisfied as to the terms of the bid, and the COB has approved the prospectus, the Chambre Syndicale declares the bid effective and the terms of the bid are published by public notice. The offeror must make it clearly known that a prospectus cleared by the COB is available, and a statement to that effect must appear in all advertisements. The offeror, however, does not distribute its prospectus to shareholders.

In the case of foreign acquisitions of more than 20 percent of a company, the Finance Ministry can object on the grounds of public interest.

The target must submit a draft prospectus for COB approval within four trading days of publication of the Chambre Syndicale's notice. The target must circulate its prospectus to all its registered shareholders. Joint offeror/target prospectuses may be used.

A simplified procedure is available to an offeror who already holds most of the target's shares and wants to obtain the remainder. This cash or exchange offer for all the target shares must be open 20 trading days.

While offers may be conditional, the COB and Chambre Syndicale have given no indication of what type of conditions are likely to be acceptable.

3. Disclosure

No regulations as yet apply governing the information to be disseminated to shareholders in the purchase of a controlling interest.

In the case of a takeover bid, strict regulations apply. The offeror and the target must publish prospectuses subject to COB review. Shareholders receive the following information, either in joint prospectuses or from the offeror and target separately:

- The terms of the bid, including date of Chambre Syndicale's notice, term of offering, minimum number of shares on which offer is conditioned, number of shares to be purchased, conditions of offer;
- Object of the bid, reasons behind the bid and the offeror's intentions;
- Offeror's holdings of target's shares;
- Information necessary to assess price, including returns on shares, market price, other elements that offeror took into account;
- Remuneration paid to intermediaries;
- Target's board of directors' opinion of the merits of the bid for the company and for the shareholders, whether opinion is unanimous,

dissenters' opinion if they request its inclusion. Directors' holdings in target, whether they intend to accept bid as regards their own shares;

- Information regarding offeror, including principal shareholders, activities; principal subsidiaries and holdings, 5 years' financials with notes, recent business progress and results; and
- Information regarding target, including all information that would be required in a prospectus for shares issued by target. (Such information includes five years' financials, names of directors, target's business and recent changes and prospects.) Indication of how company capital allocated, including details of securities held by itself, details of arrangements concerning company securities, to the board's knowledge, which might affect the outcome of bid (particularly sale or purchase commitments, sales with repurchase option.)

4. Substantive Protection

Minimum Offering Period: In the purchase of a controlling interest, the offeror undertakes to purchase all shares on the market over a period of 15 days. Takeover bid offers must be left open for at least a month.

All-holders: In the controlling interest procedure, the offeror undertakes to purchase all shares on the market. The takeover bid offer is made to all shareholders.

Best Price: In the controlling interest procedure, purchases must be made at the same price as that paid for the controlling interest itself. In a takeover bid, the offeror is required to offer the same price to all shareholders and to raise the offer price if it buys shares from the target and thus causes an increase in the market price, or if it deals in the market after the date upon which it may modify the offer price.

Withdrawal Rights: Shareholders have withdrawal rights until the last nine days of the offer.

Proration: Partial offers are permitted in takeover bids, but must be for at least 10 percent (5 percent if securities have high enough value) of equity capital. Proration is required.

Regulation of Purchases Outside Offer: Purchases outside the offer are not permitted during a takeover bid.

AUSTRALIA

Tender offers are a common acquisition technique in Australia, and have been regulated by statute since 1961. One purpose of the present regulatory scheme was to eliminate abuses under the previous regulation, such as changes in control without any offers being made for the shares of minority shareholders. The intent is to protect the interests of shareholders of target companies, by requiring adequate disclosure and time to consider an offer, as well as equal treatment of shareholders.

1. Regulation

Each state and territory (except the Northern Territory) of Australia has adopted substantially identical takeover legislation entitled the Companies (Acquisition of Shares) Code (the "Code"). Under the Code, most of the powers relating to the regulation of takeovers are conferred upon the National Companies and Securities Commission ("NCSC"). The NCSC delegates many of its powers to the Corporate Affairs Commissions ("CACs") of the various states. The Australian Associated Stock Exchanges ("AASE") also plays a part in the regulation of takeovers where the target securities are listed on the AASE exchanges, although the AASE rules on takeovers are now subordinate to the provisions of the Code.

Tender offer regulation applies to acquisitions (including exchange offers) that would result in the acquiror becoming entitled to more than 20 percent of the issued capital of a company, or increasing its ownership if it already owns more than 20 percent. Exceptions are provided, inter alia, for acquisitions approved by the target shareholders; acquisitions of not more than three percent of a company's voting shares in a period of six months; acquisitions of shares of very small companies; acquisitions made pursuant to a registered prospectus; and acquisitions made by will or operation of law. In the absence of such exemptions, regulated acquisitions of 20 percent or more of a company's securities may only be made in one of two ways: a takeover offer made under a "takeover scheme", or by a "takeover announcement" through a stock exchange. There are no rules affecting the acquisition of the first 20 percent of a company's voting securities although disclosure of holdings over ten percent is required.

2. Procedure and Filings

The takeover scheme is similar to a conventional United States tender offer. The offeror may offer cash or securities, and may seek all or only part of the target's shares. The offeror files a "Part A statement" with a copy of the proposed offer with the local CAC as the delegate of the NCSC, which will review and register the documents if they are acceptable.

The Part A statement must be delivered to the target and the stock exchange, if any, on which the target company's shares are listed, at least 14 but no more than 28 days before the offer document, which includes all information disclosed in the Part A statement, is disseminated to shareholders.

The target must furnish a recommendation (a "Part B Statement") to shareholders, either directly or by giving it to the offeror to send to shareholders along with the offer document; it is filed with the CAC upon distribution.

The offer may be conditional, but the Code prescribes the disclosures to be made regarding conditions and the manner of withdrawal. An offer may only be varied without the consent of the NCSC if the variation consists of extending the offer (although the offer cannot be open more than 12 months), increasing the consideration, or offering a cash alternative to an exchange offer.

The second acquisition procedure is the "take-over announcement." This method is not available to an offeror owning 30 percent or more of the voting shares unless the NCSC gives its consent. The offer must be for all shares of a class of stock of a listed company, and for a cash consideration. The announcement is made by a stockbroker on the floor of a stock exchange. The offer is effective 14 days after the date of the announcement. The offer price may be raised except during the last five trading days of the offer. If the price is raised, all offerees who have not sold their shares receive the increased price, but those who sold previously do not. With the NCSC's consent, the offeror can lower the price if the target has devalued the shares, for example, by declaring a dividend. The circumstances under which the offer may be withdrawn are strictly regulated. The offer cannot be conditional.

No advance filing is required in a takeover announcement. On the day the announcement is made, the offeror delivers copies of a "Part C Statement" to the target company, the CAC and the exchange upon which the target shares are listed. Within 14 days of the announcement, the offeror sends a copy of the Part C Statement to each offeree shareholder. Also within 14 days, the target company furnishes copies of a recommendation statement (the "Part D Statement") to the offeror, stock exchange, and CAC. This statement does not have to be sent to the target's shareholders.

The same procedure applies for foreign offerors, although under the Foreign Takeovers Act the Treasurer of the Commonwealth of Australia, who is advised by the Foreign Investment Review Board, must be notified of investments by foreigners exceeding 15 percent of a company's shares, and may restrict such acquisitions on grounds of national interest.

The Code also provides for compulsory offers and acquisitions. Once an offeror becomes entitled to 90 percent of the target's shares, the remaining shareholders (as well as holders of non-voting shares, options and convertible notes) must be given the opportunity to sell out at the offer price. This option must be open for three months, and the notice to the security holders must include a report of an independent expert stating that the terms are fair and reasonable. Correspondingly, a party holding 90 percent of the target as a result of an offer for all of the shares can buy out the remaining shareholders of the class for which the offer was made at the offer price.

3. Disclosure

While there are no extensive financial disclosure provisions or any financial statement requirements applicable to takeovers, it should be noted that companies legislation requires the ongoing disclosure and filing of financial information. The Part A Statement furnished by the offeror includes the following information:

- Period during which the offer is open;
- Names and addresses of directors, principal activities of corporation;
- Name and occupations of offerors who are natural persons;
- Offeror's holdings, recent dealings in target's securities, intentions regarding offers for classes of securities other than target shares;

- Where consideration includes offeror's securities, changes in offeror's (and its subsidiaries') capital structure in last 5 years;
- If consideration includes cash, source of financing;
- Details of any agreement made between offeror and target directors conditional on outcome of offer; any compensation for loss of office;
- Recent material changes, known to offeror, in target's financial position;
- Offeror's intentions regarding continuation of target's business, major changes to be made, future employment of target's employees;
- In an exchange offer, price information regarding securities offered, information about third-party issuer of exchange securities as if it were offeror; and
- Intentions to transfer target shares to other persons.

The Part B Statement furnished by the target includes:

- Directors' recommendations as to offer; dissenting directors' views;
- Details of directors' holdings of target's and offeror's securities;

- Whether directors holding shares intend to accept offer;
- Recent transactions by offeror and target in each other's shares;
- Compensation for loss of office, or upon transfer of target's property;
- Details of any other agreements in connection with outcome of offer;
- Interests of directors of target in contracts entered into by offeror;
- Recent price information as to target shares; and
- Recent material changes in target's financial position.

An independent expert's report is required in the Part B Statement where the offeror has connections with the target company (e.g., the offeror is a substantial shareholder of target, or there is a common director). This report must state whether in the expert's opinion the offer is fair and reasonable, and must set out reasons for such opinion.

The Part C Statement furnished by an on-market offeror includes:

- Names, addresses of directors, and principal activities of offeror;
- Details of offeror's holdings in target's

securities;

- Details of all recent transactions in target's and offeror's shares by offeror or its associates;
- Offeror's intentions to acquire additional target company securities, and the terms thereof; and
- Source of funds for consideration.

The Part D Statement furnished by the target company is very similar to the Part B Statement. No independent expert's report as to fairness is required.

4. Substantive Protections

Minimum Offering Period: An offer by takeover announcement is a standing offer to purchase shares for one month, extendable to six months. A takeover offer must last between one and six months (extendable to twelve).

All-holders: Offers under both takeover offers and takeover announcements must be extended to all shareholders of the class.

Best Price: In a takeover scheme, the same price must be offered for all shares. A "best price" provision also applies to an increase in consideration. If the offeror purchases shares on an exchange at a higher price than the offer price, the offer price must be increased accordingly. The price paid in a takeover announcement must be at least the highest price paid for the securities in the last four months. Market purchases made during the offer at above the offer price will result in raising the offer price.

Withdrawal Rights: Except in the case of withdrawal upon extension of the offer period beyond six months, there is no statutory provision specifying circumstances in which a shareholder may withdraw his acceptance of an offer, whether or not it was unconditional. It is not clear whether a shareholder may withdraw his acceptance of an offer subject to conditions not yet fulfilled.

Proration: Partial offers are permitted in takeover offers. The offer must either be made in the same proportion to all shareholders, or purchases must be prorated. Partial offers are not permitted in takeover announcements.

Regulation of Purchases Outside Offer: Even though an intended takeover bid has been declared, shares may be acquired without restriction before the offeror reaches the prescribed threshold. Thereafter, it may lawfully acquire shares only on the market in the ordinary course of business, and then only if it has made an on-market takeover announcement or if the Part A Statement for a takeover scheme has been served. The right to purchase on the market during takeover schemes is restricted where the offer is subject to many conditions.

It should be noted that the NCSC has the power to declare an acquisition, or particular conduct during a takeover, to be unacceptable. Such declarations are generally limited to circumstances where the offeree shareholders do not know the identity of an offeror, are given insufficient time or information to assess a proposal or are denied equal opportunity to participate in the benefits of the acquisition. The NCSC can apply to a court to impose sanctions in such cases.

SWITZERLAND

Switzerland does not regulate takeovers. The majority of Swiss companies are closely held, and thus even the general disclosure requirements for public companies are not applicable to most tender offers.

THE NETHERLANDS

1. Regulation

The Netherlands does not generally exercise control over mergers and acquisitions, but procedural provisions are embodied in a voluntary code. The Merger Conduct Rules (the "Rules"), which have no statutory basis, were promulgated in 1970 by the Social and Economic Council, an advisory body to the government composed of union, employer and government representatives. The Rules are administered by the Merger Panel, a body created by the Rules. They cover several types of acquisition, including tender offers, which are frequently used in the Netherlands.

While the Rules embody a voluntary code, they appear to be respected. Sanctions for their breach include a public censure, in which case stockbrokers are prohibited by their self-regulatory organization from participating in the offer.

The Rules apply to all offers for listed shares which are "made publicly known by the offeror" and include exchange offers. Offers made non-publicly to more than half the target's shareholders are also covered. Exemptions from the Rules may be granted. The Rules do not apply to market purchases or "creeping acquisitions" and there is no threshold at which a public offer is triggered.

2. Procedure

An offeror must first discuss the offer with the target's board. If any agreement is reached as to the offer, this must be disclosed promptly. As soon as possible thereafter, the offeror must draw up an offering document, and announce that it is available in the official gazette and other newspapers. Copies of the offering documents must be sent to the Merger Panel and the Amsterdam Stock Exchange. The stock exchange staff reviews the documents.

The directors of the offeror and target must submit to the Merger Panel statements of their and their affiliates' transactions in shares of the target (and the offeror, in the case of an exchange offer) within the last six months.

The target board must hold a shareholders' meeting at least eight days before the offer's termination date. Prior to the meeting, the board must distribute to the target shareholders a report setting out the board's position on the offer, with reasons. This document must also be submitted, at the time of publication, to the Merger Panel and the stock exchange.

The offeror must also call a shareholders' meeting in the case of exchange offers involving a substantial issuance of the offeror's securities.

The offeror may impose a limited number of conditions on its offer. Such conditions may include the acceptance of the offer by a minimum number of shareholders, the continued absence of other offers and material changes warranting withdrawal, and approval by the Merger Panel.

There are no general restrictions that would prevent an offer by a foreign offeree, although the Central Bank must approve the acquisition of more than five percent of the shares of a bank. The procedure prescribed by the Rules applies equally to domestic and foreign offerors.

It should also be noted that the Rules prescribe employer/employee relations during acquisitions. Trade unions must be notified (in confidence) of merger negotiations and impending offers and given the opportunity to express their opinions.

3. Disclosure

Minimum contents of the offering document include:

- Business and financial information regarding both the offeror and the target;
- Terms of the offer, including price;
- Minimum number of shares offered for;
- Details of target's executive board and supervisory board's compensation after consummation of offer, compensation for loss of office;
- Details of any acquisitions of target shares made by offeror in last three years from target

directors or their associates, including price and justification of any difference between such price and the offer price; and

- Details of offeror's direct or indirect holdings in target shares, and target's holdings in offeror's shares.

The stock exchange may require further information.

4. Substantive Protection

<u>Minimum Offering Period</u>: In an agreed takeover, the offer must remain open for at least 20 days. In a hostile takeover, the offer must remain open for at least 30 days. The offeror must announce whether it accepts shares tendered within five days of the expiration of the offer.

<u>All-Holders</u>: Public offers must be made to all holders of the same class of securities.

<u>Best Price</u>: The same price must be offered to all security holders under the offer but purchases may be made outside the offer.

<u>Withdrawal Rights</u>: Tendering shareholders only possess rights of withdrawal in the event that the offeror postpones the date on which it is required to announce its acceptance of tendered shares.

<u>Proration</u>: Partial offers are not permitted.

<u>Regulation of Purchases Outside Offer</u>: The Rules allow purchases to be made on the stock exchange outside the offer.

C. SPECIAL COMPLIANCE ISSUES ENCOUNTERED BY FOREIGN BIDDERS UNDER UNITED STATES REGULATION OF TENDER OFFERS

The rules and regulations under the Williams Act do not provide for special consideration to be given to foreign bidders. Both domestic and foreign bidders must operate pursuant to the same substantive and disclosure provisions of the federal securities laws. In meeting those requirements, however, the foreign bidder may face disclosure issues which do not arise when a domestic bidder makes a tender offer.

1. Jurisdiction

In making an offer for an American corporation, a foreign bidder will normally subject itself to subject-matter jurisdiction as well as personal jurisdiction in United States courts. Similarly, where a foreign corporation's securities are traded in the United States, an offer for those securities by a foreign bidder may invoke United States jurisdiction and the application of Williams Act. 3/

Application of the Williams Act to a tender offer by a foreign bidder will depend upon the facts in each transaction. In general, the courts have utilized two standards in determining if the federal securities laws have extraterritorial application: the conduct test, under which jurisdiction is predicated on conduct occurring within the United States; and the effects test, under which jurisdiction is predicated upon acts causing significant and foreseeable effects within the United States, regardless of where the conduct occurred. 4/ The courts have interpreted jurisdictional provisions broadly, "to protect domestic investors who have purchased foreign securities on American exchanges and to protect the domestic securities market from

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3/ Under Commission Rule 3a12-3, 17 C.F.R. Section 240.3a12-3, securities of foreign private issuers registered with the Commission are exempt from the reporting and proxy provisions of the Exchange Act, but not the Williams Act provisions. Foreign private issuers whose securities are held by fewer than 300 U.S. residents or who furnish the Commission with certain reports, are exempt from registration with the Commission.

4/ *See IIT v. Cornfeld*, 619 F.2d 909, 918 (2d Cir. 1980); *Schoenbaum v. Firstbrook*, 405 F.2d 200, 208-09 (2d Cir.), 405 F. 2d 215 (2d Cir. 1968) (en banc rehearing on other grounds), *cert. denied*, 395 U.S. 906 (1969).

the effects of improper foreign transactions in American Securities." 5/

Where the number of United States holders of the foreign corporation's securities is not substantial, a foreign bidder can avoid United States jurisdiction and the application of the federal securities laws by minimizing the conduct in the United States concerning the offer by, for example, not mailing the offer into the United States, not accepting any securities tendered from within the United States, and utilizing depository and transfer agents not located in the United States. The Court of Appeals for the Second Circuit has held that there is "no reason to extend jurisdiction to cases where United States activities ... are relatively small in comparison to those abroad." 6/

In Plessey Company PLC v. General Electric Company PLC, 7/ the district court held that the Williams Act did not apply to an exchange offer by a British company for the securities of another British company, even though the target corporation's securities were registered with the Commission and traded on the New York Stock Exchange. The offer expressly excluded

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5/ Schoenbaum v. Firstbrook, 405 F. 2d at 206.

6/ IIT v. Cornfeld, 619 F.2d at 920, citing Bersch v. Drexel Firestone, Inc., 519 F.2d 974, 987 (2d Cir.), cert. denied, 423 U.S. 1018 (1975).

7/ 628 F.Supp. 477 (D. Del. 1986).

United States holders and was structured to avoid the United States jurisdictional means by prohibiting the mailing of materials into the United States and the acceptance of shares tendered in an envelope postmarked from the United States. In addition, the American press was excluded from press conferences and were not provided copies of the press releases. The court found this factor significant, even though the offer was immediately and widely reported in the United States press. Of particular significance was the predominately foreign nature of the offer: 98.4 percent of the target's potential voting shares were in the hands of non-United States residents.

Foreign bidders conducting tender offers for the shares of foreign corporations which have United States shareholders often prefer to give foreign shareholders an election to receive either cash or securities of the bidder but, to avoid filing a 1933 Act registration statement in the United States, restrict United States shareholders to receiving only cash. In such situations, the question has arisen whether the offer to United States shareholders, even though limited to cash, constitutes an "offer to sell" securities within the meaning of Sections 2(3) and 5 of the 1933 Act. The staff has taken the position that it does not comprise such an "offer to sell" provided full and conspicuous disclosure is made that the securities are not being offered to United States shareholders and adequate safeguards are implemented to assure that no United States shareholder receives any of the securities. 8/

Because of the laws of other countries, this solution may not always be workable. The staff has also issued no action letters relating to the use of "vendor placings," which are often employed in acquisitions of British companies. In a vendor placing, the offeror issues its own securities to the shareholders of the acquired company, called "the vendors," in return for their shares. At the same time, the vendors renounce their right to the acquiror's shares in favor of the acquiror, which sells the shares on behalf of the vendors and remits the money to them. The shares are sold in such a manner that they "come to rest" outside the United States. The staff has taken the position that the shares issued by the acquiror to the vendors do not have to be registered pursuant to the Securities Act in light of the fact that the shareholders of

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8/ Alberta Energy Ltd. (July 19, 1982); Jamaica National Investment Company Ltd. (November 29, 1979.) Where an offer involves sufficient conduct or effects in the United States to be subject to the Williams Act, any condition excluding shareholders in a particular country would violate the Commission's "All Holders-Best Price" rules, found at Rules 14d-10 and 13e-4(f)(8). See Securities Exchange Act Release No. 23421 (July 11, 1986). Similarly, attempts to provide United States holders an alternative form of consideration are now governed by those rules. The Commission will, however, consider requests for exemptive relief from those provisions on a case-by-case basis. Id.

the company being acquired (i.e., the vendors) receive only cash and are not entitled to retain the acquiror's shares. 9/

2. Financial Information

One of the most difficult areas for a foreign bidder relates to the nature and extent of financial information required to be disclosed by the bidders. The financial statement requirements for bidders are set forth in Item 9 of Schedule 14D-1, which requires financial statements, if that bidder's "financial condition is material to a decision by a security holder whether to sell, tender or hold" the security sought in the tender offer. The financial condition of a bidder is considered "material" to the shareholders where the bidder does not otherwise file publicly available financial information and is seeking a majority or other controlling interest of a subject company. 10/ Also relevant to the determination of the materiality of the financial condition of

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9/ See e.g., Electrocomponents PLC (Sept. 23, 1982); Cambrior, Inc. (June 22, 1987); Oldcastle, Inc. (July 3, 1986).

10/ See Corenco Corp. v. Schiavone & Sons, Inc., 362 F.Supp. 939, 948-50 (S.D.N.Y.), aff'd in part, 488 F.2d 207 (2d Cir. 1973); Prudent Real Estate Trust v. John Camp Realty, Inc., 599 F.2d 1140 (2d Cir. 1979).

the bidder, is the ability of the bidder to finance the acquisition. 11/

In Life Investors, Inc. v. AGO Holding, N.V., 12/ a Netherlands corporation sought 15 percent of the outstanding stock of an American insurance company. In holding that the bidder's financial statements were material, the Court of Appeals for the Eighth Circuit focused on the fact that the tender offer, although limited to approximately 15 percent of the outstanding stock, was an amount sufficient to permit it to exercise control, but nevertheless created a minority class of shareholders retaining 40 percent of the company. The court also noted that the foreign bidder was not otherwise subject to United States disclosure obligations.

Assuming the financial condition of the foreign bidder is deemed material, "adequate" financial information concerning the bidder 13/ must be disclosed in the Schedule. Additionally, pursuant to Rule 14d-6(e)(viii), the offering

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11/ See Securities Exchange Act Release No. 13787 (July 21, 1977).

12/ [1981] CCH Fed. Sec. L. Rep. Para. 98,356 (8th Cir. 1981).

13/ If the bidder is controlled by another entity which is not a natural person and has been formed by the parent for the purpose of making the tender offer, current adequate financial information concerning such parent would be required by Item 9 of the Schedule.

circular disseminated to shareholders must contain either the disclosure required by the Item or a fair and adequate summary thereof.

To provide guidance to bidders as to what constitutes current adequate financial information, Instruction 1 to Item 9 sets forth the type of financial information which would be deemed adequate for purposes of the item. The "safe harbor" provided by Instruction 1 is premised on the nature of the bidder. For foreign bidders, financial statements prepared in compliance with Form 20-F, if the bidder would be eligible to use such form, would be sufficient. For the purpose of limiting the possible burdens on bidders who are not subject to the periodic reporting requirements of the Exchange Act, Instruction 3 to the Item permits the use of unaudited financial statements if audited statements are not available or obtainable without unreasonable cost or expense. If a bidder relies upon this instruction, the bidder must include a statement to that effect and disclose the reasons therefor in its response to Item 9.

Not only must a foreign company's financial information be presented in response to Item 9 of the Schedule, that information must be presented in a manner that is meaningful to the United States security holder so that an informed investment decision can be made. Accordingly, the staff has taken the position that disclosure of a bidder's financial information expressed in foreign currency terms is deemed not responsive to the Item requirement unless that information is accompanied with appropriate disclosure of the bidder's accounting practices together with the identification and, if practicable, quantification of any material variation in those accounting practices from United States GAAP and the form and content of Regulation S-X.

3. Disclosure of Foreign Regulatory Requirements And Controlling Persons

Another issue creating special concerns for the foreign bidder relates to foreign law. Item 10(b) of Schedule 14D-1 requires, where material and to the extent known by the bidder after reasonable investigation, disclosure of any "regulatory requirements which must be complied with or approvals which must be obtained in connection with the tender offer." In addition to securing approval from certain United States regulatory agencies, a foreign bidder might also be subject to regulatory controls emanating from its home country. This would include the obtaining of consents under exchange control regulations. Moreover, certain foreign jurisdictions may place restrictions on the manner in which a company controls a foreign entity. 14/ Such restrictions must be adequately

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14/ See General American Host Corporation v. Triumph American, Inc., 359 F.Supp. 749 (S.D.N.Y. 1973), wherein the court states that "[f]oreign controls,
(continued . . .)

disclosed. Conflicts also arise when foreign law forbids the disclosure of certain information required to be disclosed pursuant to Schedule 14D-1 and disseminated to shareholders in accordance with Rule 14d-6(e)(1)(vii). 15/

(. . . continued)
particularly when they differ in extent and kind from controls the United States investor has come to expect from the United States government in relation to domestic operations, are matters which should be called to the attention of shareholders in a tender offer.

15/ In one such situation, a Canadian bidder was making a cash tender offer to United States shareholders of another Canadian company. The bidder had borrowed funds for the offer from a Canadian chartered bank. The Canadian bank was not a "bank" as defined in Section 3(a)(6) of the Exchange Act and, accordingly, the bidder was required by Item 4 of Schedule 14D-1 and Rule 14d-6(e)(1)(vii) to disclose the name of the bank in the offering circular. Counsel for the bidder, however, represented that such disclosure would violate Section 310(2) of the Bank Act (Canada), which states that "(e)very person who uses the name of a bank or a foreign bank in a prospectus or advertisement for a transaction related to securities . . . is guilty of an offense against this Act . . ." In order to permit the bidder to comply with this Canadian legal requirement and at the same time make the name of the bank available to persons in the United States who may wish to know it, the staff issued a "no-action" position to the bidder indicating that the bidder need not identify the bank by name in the offering circular, provided the bank was named in response to Item 4 of Schedule 14D-1; a complete copy of the loan agreement was filed as an exhibit to the Schedule; all material facts regarding the loan, other than the name of the bank, were disclosed in the offering circular; and the offering circular contains a statement that the name of the bank has been disclosed in the Schedule 14D-1 filed with the Commission. Alberta Energy Ltd. (July 19, 1982).

Item 2 of Schedule 14D-1 calls for, inter alia, the identity of the offeror and its place of organization and principal business. This information must also be given with respect to each person controlling the offeror. This can raise special problems for the foreign corporation, since identification of the controlling persons of a foreign bidder may be obscured by holding companies or by the existence of bearer shares. 16/

4. United States Regulatory Restrictions on Foreign Acquisitions

A significant restriction on tender offers that applies to foreign and domestic bidders alike, is the United States antitrust laws. These laws apply to foreign companies if they do business in the United States or if their activities have an effect on United States commerce.

The Hart-Scott-Rodino Antitrust Improvement Act of 1976 imposes a waiting period on all acquisitions meeting certain threshold requirements to allow officials at the Department of Justice and the Federal Trade Commission to examine the antitrust implications of the takeover. The Act contains

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16/ See Ronson Corporation v. Liquifin Aktiengesellschaft, 483 F.2d 846 (3rd Cir. 1973).

several exemptions, including Section 802.51 of the rules, 17/ which deals with acquisitions by foreign persons. Under that rule, the acquisition by a foreign company of a United States company with annual net sales and total assets of $25 million or less is exempt from the reporting requirements and the waiting period. Acquisitions by a foreign company of another foreign company is also exempt if the sales and assets of the two companies in the United States total less than $110 million.

Restricted Industries: There are a number of federal and state statutes that prohibit or restrict the ability of foreign corporations to acquire control or to exceed a specific ownership interest in certain industries. 18/ These include banking, communication, shipping, nuclear energy, defense industries, and mineral and natural resources. If the restricted industry constitutes only a limited portion of the subject company's operations, the bidder might be able to resolve its regulatory problems by divesting itself of the restricted industry or placing the restricted industry in the hands of an independent trustee pending federal agency

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17/ 16 C.F.R. Section 802.51.

18/ See Fleischer & Feder, Special Problems of Foreign Bidders in Acquisitions by Tender Offer, 1 J. Comp. Corp. L. & Sec. Reg. 349, 353 (1978).

approval. 19/ For the most part, however, the United States historically has encouraged foreign investment in this country. 20/

19/ Id., at 353.

20/ See Berger, Applying Uniform Margin Requirements to Foreign Entities Attempting to Acquire U.S. Corporations, 24 Va. J. Int'l L. 543 (1984).

VI. ISSUES RAISED BY INTERNATIONAL OR MULTINATIONAL SECURITIES OFFERINGS

Securities markets around the world are changing as foreign issuers expand their use of United States capital markets, domestic issuers access foreign markets and both debt and equity offerings are made multinationally. As a result of these offerings, the lines of demarcation between domestic and international capital markets are beginning to blur and domestic markets are facing serious competition from a largely unregulated, transnational financial market.

The changes in these lines raise numerous issues under United States securities laws for domestic issuers raising capital offshore and foreign issuers selling to United States investors, at home or abroad. Questions concerning the extraterritorial application of Section 5 of the Securities Act have resulted in complex and costly offering procedures to assure that registration provisions do not apply, as well as the exclusion of United States persons from various offshore investment opportunities. Yet, large offshore trading markets have developed, where United States investors who choose to buy unregistered securities are free to do so, but only after certain periods of time following an offering of the securities. This distinction has on occasion proved costly to United States investors.

Foreign issuers that consider directly accessing the United States capital markets through registered public offerings are frequently dissuaded by the substantial differences in disclosure requirements, particularly with respect to accounting principles and auditing standards. As registration under the Securities Act brings with it a periodic reporting requirement under the Securities Exchange Act, a foreign issuer deciding whether to register securities must also consider the continuing reporting costs. Concerns about liability provisions, perceptions of a litigious environment and submission to SEC oversight also contribute to foreign issuers' reluctance to enter voluntarily the United States securities markets.

The challenge is to remove unnecessary impediments to transnational capital formation, while assuring that those buying securities in the United States capital markets are afforded the protections intended by the Securities Act and the Securities Exchange Act. Care needs to be taken as an integral part of this effort to avoid accommodations to foreign corporate practices and laws that unduly advantage foreign issuers over domestic issuers.

A. EXTRATERRITORIAL APPLICATION OF UNITED STATES LAW

1. Redefining the Reach of Section 5

For companies raising capital abroad, the principal issue under the federal securities laws is the reach of the registration requirements under Section 5 of the Securities Act across national boundaries. As early as 1964, the Commission recognized that application of the registration provisions of Section 5 of the Securities Act should be more restricted than the Act's full jurisdictional reach. 1/ The Commission has not sought to apply the registration provisions to transactions using jurisdictional means but not involving United States persons or markets. In certain circumstances, even sales to non-United States persons made within United States markets have been considered beyond the scope of the registration provisions. 2/ However, the demarcation of the appropriate reach of Section 5 has not been definitively determined. While the issue has existed for many years, it has become of critical importance with the development and maturity of major markets offshore and the huge growth of transnational investment. In defining the

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1/ Securities Act Release No. 4708; 29 Fed. Reg. 9828 (July 1, 1964). In that release, the Commission took the position that it would not take enforcement action if securities are sold under circumstances reasonably designed to prevent the distribution or redistribution of the securities into the United States or to United States persons.

2/ See, e.g., Israel Discount Bank (July 23 and Sept. 13, 1981); Bank Leumi (May 7, 1982).

jurisdictional ambit of registration, the implication of the secondary trading markets must be fully considered. Sales of securities abroad by an issuer may raise Section 5 questions, while sales of these same securities a few months later in the secondary market do not implicate the United States securities laws at all. This dichotomy occurs because, pursuant to the Securities Act, registration is generally required for offers or sales of new offerings of securities by issuers or affiliates, while secondary trades are exempt from registration under the Securities Act. The Securities Exchange Act, which requires periodic reporting of information by issuers with securities traded in United States markets, does not extend to foreign securities traded only in foreign markets. 3/

3/ Pursuant to Sections 12(b) and 12(g) of the Securities Exchange Act, 15 U.S.C. Section 78l(b), (g), issuers with securities registered on a national securities exchange, or engaged in interstate commerce, in a business affecting interstate commerce or with securities traded by use of any instrumentality of interstate commerce and with more than 500 shareholders of record and $5 million in assets, must register those securities under the Exchange Act. Foreign issuers with fewer than 300 United States security holders are exempt from the provisions of Section 12(g). In addition, foreign issuers whose securities are not traded on an exchange or quoted on NASDAQ may claim an exemption from Section 12(g) pursuant to Rule 12g3-2(b), 17 CFR Section 240.12g3-2(b), if they file with the SEC the documents they are required to make public in their home jurisdiction. Certain issuers whose securities were quoted on NASDAQ prior to October 5, 1983, may also rely on the exemption.

This free accessability of United States persons to securities in the foreign secondary markets causes a problem for United States investors when foreign issuers make rights or exchange offers. United States investors have made purchases in offshore trading markets in great volume. As a result, there are a number of foreign companies that have never voluntarily entered the United States securities markets, but whose securities are held by United States persons in the United States. Those holding foreign securities originally purchased in foreign secondary markets may be precluded from participating in rights or exchange offerings because the foreign issuer is reluctant to register the offerings as is generally required by the Securities Act. Rather than registering the securities, the foreign issuer either excludes United States holders or provides them cash instead of securities. Either alternative can be costly to United States holders.

The recent development of active international trading markets and the significant increase in offshore offerings of securities, as well as the significant participation by United States investors in foreign markets, have heightened the need to revisit the parameters of the registration provisions in order to address these inconsistencies. 4/

4/ The problems raised by application of United States registration requirements in a foreign context are illustrated by the following situation recently addressed by the Commission. In connection with a

As the international markets have expanded, the differing treatment of United States persons in primary and secondary markets has become more pronounced and has affected a large number of persons. United States investors have expressed discontent with their exclusion from investment opportunities caused by application of the securities registration requirements to foreign issues. Issuers, both domestic and foreign, have been dissatisfied with the complex procedures required to assure that securities sold

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number of recent registered offerings by foreign companies, a question was raised as to whether continuous registration would be required because affiliates of the issuer engaged in market-making activities in the foreign markets, and persons purchasing in the foreign markets for resale into the United States might be underwriters. _See_ Section
(continued . . .)

(. . . continued)
2(11) of the Securities Act, 15 U.S.C. Section 77b(11). If registration were required, a foreign issuer whose affiliate is conducting activities solely in a foreign jurisdiction would be required to register securities in the United States solely because a United States market for the securities exists. The Commission decided not to apply the registration requirements, however, if the issuer is a foreign company with securities registered under the Exchange Act, its principal market is in a foreign country and not more than 20 percent of its average trading volume is in the United States. In addition, disclosure of the market participation was required to be included in filings made under the Securities Act and the Exchange Act; there could be no special selling efforts in the United States targeted to effect a distribution in this country and sales by the affiliate were required to be made in the normal course of market activities recognized as legal and appropriate in the issuer's home country.

abroad are not sold or resold to United States persons. 5/ As a matter of comity, it is questionable whether United States laws should require foreign issuers making primary offerings in foreign markets in accordance with the laws of that foreign jurisdiction to take extensive precautions to assure the securities are not sold to United States persons, as often happens.

There appears to be a broad-based consensus that Section 5 properly applies to offerings made in the United States capital markets. 6/ This territorial approach to the regulatory provisions of the Securities Act is consistent with the regulatory ambit of the Securities Exchange Act and with comity principles. Such an approach recognizes the primacy of the laws in which a market is located. As investors choose their markets, they would choose the laws applicable to such markets. Such an approach does not, however, affect the broad reach of

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5/ See, e.g., Proctor & Gamble (Feb. 21, 1975), outlining the procedures followed for Eurobond offerings.

6/ For example, in February 1987, the Commission held a roundtable with representatives of the bar, issuers, investors and securities professionals to discuss internationalization of the securities markets. The participants favored the territorial approach.

antifraud provisions of either the Securities Act or the Securities Exchange Act as presently applied. 7/

Pursuant to the territorial approach, United States securities laws would protect all participants in the United States capital markets, including foreign persons in the United States. The distinction between treatment of United States investors when they purchase in primary offerings and when they purchase in foreign secondary markets would be greatly reduced, because the primary consideration in applying United States disclosure regulations to sales in the primary and secondary markets would be whether the offer or sale is made within the United States. Offshore offerings targeted at United States investors or intended to evade United States securities laws would continue to be fully regulated.

With respect to issuers, both domestic and foreign, which offer securities abroad and have active United States trading, the periodic reporting requirements of the Securities Exchange Act can assure that United States investors who buy securities offered abroad that flow back to the United States are provided the same information that would be provided by the registration process. The integrated disclosure system for domestic, as well as foreign, companies that file Securities Exchange Act

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7/ *See* discussion in Chapter VII, *infra*.

reports already permits seasoned companies to incorporate by reference Securities Exchange Act reports into Securities Act filings. 8/ The territorial approach would place even greater reliance on the periodic reporting system mandated by the Securities Exchange Act.

In defining a territorial approach, the concept of an "offer or sale within the United States" must be developed, taking into account advancing technology and worldwide telecommunications. Clear, simple guidelines designed to assure that investors in United States capital markets have appropriate information available to them must be established, taking into account the differences in debt and equity offerings 9/ as well as the differences in the types of purchasers that may be involved. 10/

8/ *See* Forms S-2, S-3, F-2 and F-3. 17 CFR Section 239.12, .13, .32 and .33.

9/ Differences between debt and equity have often been recognized in setting disclosure requirements. For example, issuers that file reports under the Exchange Act may incorporate those reports by reference into Securities Act filings when selling investment grade debt, while incorporation by reference is permitted for primary issuances of equity securities only if certain other tests are met. *See* Form S-3; Instr. I.B.; 17 CFR Section 239.13.

10/ Congress recognized a distinction between institutional and sophisticated investors on the one hand, and the investing public on the other, when enacting the Securities Act. *See* Landis, "The Legislative History of the Securities Act of 1933," 28 G. Wash. L. Rev. 29, 37 (1959). This distinction has subsequently been recognized by the Commission

2. Recent Interpretations

Several recent interpretive and no-action letters address issues raised by the transnational trading of securities. For example, a letter to College Retirement Equities Fund ("CREF"), 11/ addressed the concern of United States institutional investors that they were being excluded from foreign offerings, even though they should have been able to purchase in a private placement exempt from registration under the Securities Act. Foreign issuers excluded these institutions to avoid any question about the application of the registration provisions to the offshore offering. While the Commission in earlier releases had indicated that the private placement and offshore offering would not be integrated, foreign issuers remained concerned. The staff issued this interpretive letter to squarely address the issue and stated that offshore offerings made to non-United States persons will not be integrated with private placements. The letter made clear that the foreign issuers

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and the staff in various contexts. See, e.g., Securities Act Releases No. 6188, 45 Fed. Reg. 8960 (Feb. 11, 1980) and 6508, 49 Fed. Reg. 5920 (Feb. 10, 1984).

11/ Feb. 18, 1987.

would not be required to take any precautions to assure that the foreign portion would come to rest abroad in addition to those, if any, they would take if the United States placement were not made. A similar letter was issued to CREF on June 4, 1987, relating to CREF's ability to participate in rights offerings and exchange offers.

In the first letter to CREF the staff also stated its view that the securities purchased by United States institutions could be resold onto the Paris Bourse without inquiry as to the citizenship or residence of the purchaser on the Bourse, provided sales were made in regular way transactions. In view of the limited United States investor participation on the Bourse, such a resale, which would not be directed at United States persons, does not call for application of the registration provisions.

Counsel for the French Government requested a no-action position respecting the French privatization program in which substantial interests in entities held by the French Government are being sold to the public. The French had concerns similar to those expressed in the CREF letters that, if a United States private placement were made as part of a privatization offering, additional procedures would be required to assure that sales would not be made to United States persons as part of the foreign offering. Additionally, the procedures mandated by French law required that offers be made to all French residents without regard to citizenship. As a result, there was a concern that the registration requirements of the Securities Act could be violated by unregistered sales to United States citizens residing in France. The staff stated it was of the view that the United States private placements would be considered separate from the French portions of the offerings and additional procedures would not be required in the French offerings to assure sales were not made to United States persons. In addition, in view of the mandate by French law to sell to United States persons, the staff stated it would not take action if the French portions of the offerings were carried out as required by French law even though sales might be made to United States citizens residing in France. 12/

B. ACCESS TO UNITED STATES MARKETS BY FOREIGN ISSUERS

Facilitating foreign issuers' direct access to the United States capital markets presents far more difficult challenges. The needs of investors in the United States markets are largely the same whether the issuer is domestic or foreign. The costs of compliance for selling the same type of securities to the same class of investors should not be significantly greater for domestic public companies

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12/ French Privatization Program (Apr. 17, 1987).

than for foreign companies. Whatever modifications in disclosure requirements are made to recognize home country laws and practices, the liabilities for such disclosure are provided by the Securities Act and Securities Exchange Act and apply equally to foreign and domestic issuers. Nonetheless, foreign issuers' reluctance to access the United States markets cannot simply be dismissed. United States investors want to purchase such securities and will go offshore to do so. This can adversely affect the ability of United States markets to compete with foreign markets as well as be costly to United States investors.

Central to the United States disclosure system are the required financial statements and related financial disclosure. Differences in accounting principles, auditing standards and auditor independence standards are the principal impediments to foreign issuers' publicly offering securities in the United States. Reconciliation of foreign accounting disclosure to United States accounting principles can be done, but may be time consuming and costly. Compliance with auditing standards can be very costly, and if it has not been done in past periods, may not be possible. Nonetheless, since the accounting principles and auditing standards are at the core of the disclosure system, accommodation of foreign standards and practice has been limited pending evolution of international accounting and auditing standards. That process is ongoing. 13/

Foreign issuers also have raised concerns about liabilities imposed by the United States securities laws and about submission to the jurisdiction of the SEC. Perhaps these concerns will lessen as home country markets mature, home country regulatory bodies become more active and mutual surveillance and enforcement agreements are developed and used. 14/

As an initial, experimental effort the Commission is developing a proposal for reciprocal disclosure for the registration of specified securities. The reciprocal registration statement forms would use the offering document required in an issuer's home country as the prospectus for offerings in the United States. 15/ The key to implementation of the approach is accounting principles and auditing standards. If a reciprocal approach is adopted, these areas will be central in determining which

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13/ *See* discussion in Chapter IV, *infra*.

14/ *See* discussion in Chapter VII, *infra*.

15/ Of course, the offeror must comply with any state law requirements that may be applicable.

jurisdictions should be included and what classes of issuers and types of securities should be permitted.

The Commission proposed initially to implement the reciprocal approach with the United Kingdom and Canada, because the disclosure and accounting practices of those countries are most similar to those of the United States, and because of familiarity with those countries' standards due to the frequency of their issuers' filings in the United States. 16/ Reciprocal registration would apply primarily to world class issuers of investment grade debt, because those securities would trade, in large part, on yield and rating. Thus, reconciliation of accounting and auditing from the home country presentation would not be essential. In addition, limited rights offers and exchange offers may be permitted on these forms. Extending reciprocal registration to rights and exchange offers by a non-reporting foreign issuer with limited United States security holders is intended to encourage the inclusion of United States investors in such offers by facilitating the registration process. As noted above, currently United States investors are simply excluded or cashed out.

Other rulemaking efforts, not directly targeted at international issues, also may affect foreign issuers' access to the market. Small issuer exemptions under

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16/ Securities Act Release No. 33-6568 (Feb. 28, 1985).

Section 3(b) of the Securities Act, in addition to helping small issuers in the United States, may provide assistance to foreign issuers with United States employees or security holders. The Commission recently proposed Rule 701, which would exempt offerings of securities to employees under compensation plans or contracts up to $5 million if the issuer is a non-reporting company. 17/

Similarly, the staff is considering proposal of an exemptive rule under Section 3(b) of the Securities Act for rights offerings and possibly for exchange offerings of less than $5 million made by non-reporting companies. Such a rule may be useful to enable United States persons to participate in certain categories of offerings made by issuers organized in countries not party to reciprocal forms or by issuers that may be reluctant to use the forms.

A contemplated codification of interpretations under the Securities Act to clarify when institutions may resell unregistered securities to other institutions may reduce the cost of private placements. This may encourage foreign issuers to access the United States through the private placement mechanism.

17/ Securities Act Release No. 6683, 52 Fed. Reg. 3015 (Jan. 16, 1987).

A key factor in facilitating foreign issuers' access to the United States capital markets is a coordinated effort with state securities regulators. Foreign issuers entering the United States capital markets must be equally concerned with the requirements of state securities laws. Discussion has been undertaken between the SEC staff and representatives of state securities regulators.

These issues will continue to be considered as the internationalization process continues.

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