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# 2019 Guide to Foreign Private Issuer status:

## How to preserve it and what it provides to non-US companies

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A company organized outside the United States that is subject to provisions of the US federal securities laws receives substantial benefits if it qualifies as a "foreign private issuer" (an **FPI**).

- Disclosure obligations and other significant obligations are imposed on a company and on the company's officers, directors and 10 percent shareholders (1) under the US Securities Act of 1933, as amended (the **Securities Act**) and (2) under the US Securities Exchange Act of 1934, as amended (the **Exchange Act**). If a company qualifies as an FPI, then the company and its officers, directors and 10 percent shareholders do not have to comply with certain of these obligations.

- Failure to qualify as an FPI would adversely affect a company's ability to rely on Regulation S for an exemption from registration under the Securities Act for offerings and sales of equity securities conducted outside the US. Failure to qualify as an FPI could adversely affect the company's current and former officers, directors and employees by restricting their ability to resell shares that they acquire under incentive compensation plans.

- If a company that qualifies as an FPI is the target in a tender offer or takeover bid or is a party to a merger or amalgamation, then various requirements otherwise imposed under the Securities Act or the Exchange Act may not apply under certain conditions.

- An FPI that lists securities on a US stock exchange receives FPI accommodations under certain rules of the New York Stock Exchange (**NYSE**) and The Nasdaq Stock Market (**NASDAQ**).

This document:

1. Explains the tests applied in **Determining FPI status** and describes the facts that may result in a change to FPI status; these tests are important to remember, especially as a company approaches its date for determining FPI status and

2. Discusses in greater detail **Various benefits of FPI status and consequences of losing it**, specifically looking at certain consequences relating to:


   — **Registration under the Securities Act or under the Exchange Act**
   — **Offerings outside the US; Regulation S and resale restrictions**
   — **Treatment of shares issued under incentive compensation plans**
   — **Communications during an offering**
   — **Reporting and other obligations under the Exchange Act**
   — **Cross-border acquisitions; dealing with US shareholders**
   — **Listing on a US stock exchange**

In this document, we refer to a corporation or other organization as a "company" or an "entity" or sometimes an "issuer."

This document does not address an entity that is a government (which cannot be an FPI) or an entity that is required under US federal securities laws to be registered as an "investment company." This document deals with operating companies and does not address asset-backed issuers of securities, blank check companies, shell companies and certain other special types of entities. The circumstances of any particular entity may be relevant when applying many of the points in this document.

While there are specific requirements contained in many provisions of the US federal securities laws, there also are many provisions in the statutes and rules that are <u>principles</u> and require analysis when applied to particular facts. Also, in the case of exemptions to various requirements under the federal securities laws, such as exemptions to the requirement under the Securities Act to register and provide specified disclosures regarding offers and sales of securities, these exemptions may not be available if their use in the particular situation is viewed as inconsistent with the principles of the federal securities laws. The SEC has some broad tools available to it (such as the general anti-fraud provisions of Section 10(b) and Rule 10b-5 under the Exchange Act) if the SEC staff wants to challenge actions that may, in the staff's view, be potentially harmful to US investors or US capital markets, whether or not the actions appear to be permitted by specific provisions of the federal securities laws.

This document summarizes certain aspects of the US federal securities laws. It does not address any provisions of any state securities laws that might apply due to conduct in a particular state or dealings with residents of a particular state.

Please note that this document is not legal advice and does not create an attorney-client privilege. This document frequently uses the term "generally" in discussing provisions of the federal securities laws and how they may be applied. Even where the qualifier "generally" is not used, please assume that application of any requirement, exception or other term of the federal securities laws will ultimately depend on the particular situation.

## Determining FPI status

An entity will be an FPI if it:

1. is a corporation or other organization incorporated or organized under the laws of any country outside the US (generally including the laws of a jurisdiction, such as a state or province, within a country outside the US),
2. is <u>not</u> a foreign government and
3. satisfies at least one of the two tests described below (the Non-US Share Ownership Test and the Non-US Business Connection Test).

The determination of a company's status as an FPI may change as the facts change over time.

FPI status is determined (the **FPI Testing Date**) annually as of the **<u>last business day</u>** of the company's most recent **<u>second fiscal quarter</u>**. So for companies whose fiscal year is a calendar year, the <u>determination date this year is June 28</u>. But in the case of a company filing an <u>initial registration statement</u> with the SEC (under the Securities Act or the Exchange Act), the FPI Testing Date will instead be a date within 30 days prior to the company's filing of its initial registration statement (and then subsequently would be the last business day of each subsequent second fiscal quarter).

A non-US company is generally free to maneuver itself so that as of the FPI Testing Date, it satisfies the tests described below that determine FPI status.

The US Securities and Exchange Commission (**SEC**) generally does not make its own assessment of FPI status, although the SEC could question or challenge a company's determination in connection with the SEC's review of a company's filings.

If an FPI loses its FPI status, it can regain FPI status again at a subsequent FPI Testing Date.

The FPI definition set out in the rules under the Securities Act and under the Exchange Act contains the following **tests** to determine whether a non-US company qualifies as an FPI as of the FPI Testing Date:

1. the percentage of voting securities owned by persons who are US residents (looking through nominee accounts to the underlying beneficial owners) (the **Non-US Share Ownership Test**) and

2. the degree of US business and operational contacts (the **Non-US Business Connection Test**).

A corporation or other organization that is incorporated or organized under the laws of a country outside the US and is not a foreign government will be an FPI unless it fails to satisfy **BOTH** of these tests. In other words, in order to qualify as an FPI, a non-US company **must satisfy at least one of these two tests**.

## Applying the Non-US Share Ownership Test

A non-US company **will satisfy the Non-US Share Ownership test** if, as of the FPI Testing Date, no more than 50 percent of its outstanding "voting securities" are directly or indirectly owned by residents of the US. "Voting securities" means securities the holders of which are presently entitled to vote for the election of directors.

In satisfying this test, the company must "look through" the ownership of brokers, dealers, banks and other nominees holding the company's voting securities to determine the residence of the underlying customers for whom the nominees are holding the shares. The company does not count voting securities that are obtainable upon the exercise or conversion of other securities (such as options, warrants and convertible securities).

Companies with more than one class of voting securities can apply the test either (1) on the basis of the percentage of the voting power held for all of the voting classes combined or (2) on the basis of the percentage of the number of securities held for all of the classes combined. The methodology chosen should be used consistently from year to year.

Regarding residency, the SEC has stated that an individual with "permanent resident status" in the US (a Green Card holder) is presumed to be a US resident. Other individuals who are not permanent residents may also be residents of the US. A company must determine what factors it will use to assess residency and should apply those factors consistently. Examples of factors that could be used include tax residency, citizenship or nationality, mailing address, physical presence, the location of a significant portion of a person's financial and legal relationships and immigration status.

For the residency of an entity, a company should generally look at either (1) the jurisdiction of formation or incorporation or (2) the principal place of business for the entity. The company should apply its choice of these two criteria consistently for all entities and from year to year.

The "look through" inquiry to determine US shareholdings may not produce completely accurate results, but it can provide an approximation. The look through inquiry need only occur with respect to brokers, dealers, banks and other nominees located in the US, in the company's jurisdiction of incorporation and in the jurisdiction where the primary trading market for the company's voting securities is located. The company must make a good faith effort to obtain information from brokers, dealers, banks and other nominees concerning the residence of the underlying shareholders. That involves identifying these nominees on the participant lists for the company's voting securities as reported to the company by depository and clearing trading systems.
If, after reasonable inquiry, the company is unable to obtain information from a nominee concerning the nominee's customer accounts (including in situations where the nominee would charge unreasonable fees to provide that information), the company

may rely on a presumption that the underlying customers are residents where the nominee's principal place of business is located. In addition, the company would have to consider information concerning US ownership of voting securities from any reports that are publicly filed or otherwise provided to the company and would have to consider any actual knowledge the company may have concerning its shareholders.

Since the location of shareholdings may change over time, it is generally safer, especially for a company (including many Canadian companies) that already has substantial US shareholdings or a US institutional following, to rely on satisfying the Non-US Business Connection Test, discussed below, rather than just relying on satisfying the Non-US Share Ownership Test. A failure under both the Non-US Share Ownership Test and the Non-US Business Connection test would result in the company no longer being an FPI.

## Applying the Non-US Business Connection Test

The analysis under the Non-US Business Connection Test consists of three distinct tests (listed below). In order to **satisfy the Non-US Business Connection Test**, a non-US company must satisfy each and every one of these three tests as of the FPI Testing Date. A company will **satisfy** the Non-US Business Connection Test if:

1. A majority of its executive officers are **not** US citizens or residents **and** a majority of its directors are **not** US citizens or residents **and**

2. Not more than 50 percent of its assets are located in the US **and**

3. Its business is not administered principally in the US.

**1. *Citizenship and residency of executive officers and of directors***

This test has two separate parts, looking at a majority of the executive officers and separately looking at a majority of the directors to determine if a majority of either group are a combination of US citizens or US residents. Failure for either group means that the Non-US Business Connection Test is failed.

For purposes of the citizenship and residency test:

- "Executive officer" is defined as the president, any vice president in charge of a principal business unit, division or function (such as sales, administration or finance), any other officer who performs a policy making function or any other person who performs similar policy making functions for the company. In addition, executive officers of subsidiaries may be deemed to be executive officers of the parent company if they perform policy making functions for the parent company.

- "Directors" refers to the directors having US-style oversight responsibility or the persons performing similar functions for the entity. If there are two boards, the relevant board is the one that more closely performs the functions of a US-style board of directors. If those functions are divided between the two boards, then the directors part of the test can be applied by aggregating the members of both boards.

For purposes of this test, a person holding dual citizenship from both the US and a non-US jurisdiction is counted as a US citizen. Determination of "residency" is discussed above under "Applying the Non-US Share Ownership Test."

**2. *Location of assets***

A company must determine whether at least 50 percent of its tangible and intangible assets are located outside the US. The SEC has not provided specific guidance regarding how to measure or determine the location of assets but has stated that a company can use the geographic segment information developed in the preparation of its financial statements or any other methodology that is reasonable and consistently applied.

**3. *Administration of business***
A company must determine whether or not its business is administered principally in the US. In making this determination, the company should assess on a consolidated basis the locations from which its officers, executives, managers and partners direct, control and coordinate the company's activities. Relevant facts might include: (i) the locations of principal business segments or operations, (ii) the locations of the company's most influential executives when they act for the company, (iii) the locations of board and board committee meetings and of annual shareholders' meetings and (iv) the locations of global and regional headquarters. Generally, no single factor is determinative.

## Various benefits of FPI status and consequences of losing it

As noted above, FPI status provides substantial benefits to a Company. One might wonder: What added benefits does FPI status really provide to an entity already organized outside the US? Under the US federal securities laws, FPI status is basically what defines an entity as a non-US entity. Without FPI status, an entity will be regulated like a US domestic company.

The advantages of being an FPI are summarized below. This does not purport to be an exhaustive listing of every possible benefit or difference that would apply if a company is treated under the US federal securities laws as an FPI.

### Registration under the Securities Act or under the Exchange Act

If a company offers its securities in the US or to US residents, and no exemption is available, that will generally require registration under the Securities Act. Also, if a company decides to list its securities on the NYSE or NASDAQ, that will require registration under the Exchange Act. Being an FPI provides a non-US company with more favorable (less burdensome) disclosure requirements in the case of either registration, as explained further below.

***a) Registration statements and disclosure generally***
**Public offerings**: If a company wants to conduct a registered offering of securities in the US to raise capital rather than conducting an exempt offering (such as a Rule 144A placement), the company would file a registration statement with the SEC under the Securities Act covering the offer and sale of the particular securities. There also are many other types of offerings or sales of securities that might require registration under the Securities Act or an exemption from registration. The Securities Act takes a broad view of: (1) what constitutes a "security" and (2) when there is an "offer" or "sale" "for value" of a security requiring either registration or an exemption from registration. If a company filing a registration statement is an FPI, it can use the appropriate F-form registration statement that provides various disclosure accommodations for FPIs from what would be required by full US disclosure requirements. If the company is not an FPI, then it would have to use the registration statement forms and disclosure rules that are applicable to US domestic companies, which will generally result in greater disclosure regarding compensation, among other matters.

**Listing on a US stock exchange**: If a company lists securities on a US stock exchange, such as the NYSE or NASDAQ, then the company will need to file a registration statement for that class of securities with the SEC under the Exchange Act. If the company is an FPI, it can use a Form 20-F registration statement that contains various disclosure accommodations from what would be required by full US disclosure requirements for a US domestic company. If the company is not an FPI, then it would have to use the registration statement form and disclosure rules that are applicable to US domestic companies. (Registration under the Exchange Act is also generally required when the numbers of global holders and of US holders of a class of equity securities reach certain thresholds, unless, in the case of an FPI, the Rule 12g3-2(b) exemption available only to FPIs is used. This point and the triggers requiring registration under the Exchange Act are described below under "Reporting and other obligations under the Exchange Act – Circumstances under which a company is required to report under the Exchange Act.")

**ADRs**: While the securities of Canadian companies are traded directly in the US, FPIs from most countries other than Canada use American Depositary Receipts (**ADRs**) for US trading purposes. An ADR is a receipt for a negotiable interest (**American Depositary Shares** or **ADSs**) in a deposit account holding the FPI's shares. (The terms ADRs and ADSs are often used interchangeably.) A US bank serves as the depositary bank and issues the ADRs. ADRs trade in the US in US dollars (and pay US dollar dividends). Trading in ADRs clears on US clearing systems. Generally, ADRs can be exchanged for the underlying shares and shares of the relevant class of the company can be deposited to obtain ADRs. If the ADRs are used just to establish trading in the underlying shares over-the-counter in the US (directly between broker-dealers and not on a stock exchange), that would be an unsponsored ADR program. In that case, a simple Form F6 registration statement under the Exchange Act is used regarding the depositary arrangement in order to permit trading. (Where the issuer is not otherwise reporting under the Exchange Act, it must rely on the Rule 12g3-2(b) exemption and as a result, must publish the information required by that Rule.) If the ADR program is going to trade on a US stock exchange, then a registration statement must be filed by the issuer under the Exchange Act (using Form 20F for an FPI). If the ADRs are also used to raise capital in the US, then the underlying shares also require a separate registration statement under the Securities Act for the offering and sale of interests in those underlying shares. This document does not address the obligations of the bank depositary issuing ADRs.

**Confidential review**: FPIs may be able to submit their initial registration statement to the SEC preliminarily on a confidential basis, while companies that are not FPIs can generally only do that if they qualify as "emerging growth companies" (generally meaning that the previous year's gross revenues were less than US$1.07 billion and the company had not sold common equity securities under an SEC registration statement as of December 8, 2011).

*b) MJDS for eligible Canadian FPIs*

A Canadian FPI may be eligible to use the favorable Canada-US multijurisdictional disclosure system (**MJDs**). MJDS provides substantial time and cost savings to eligible companies by reducing the burden of complying with US disclosure requirements. Under the MJDS system, eligible Canadian FPIs can generally use their Canadian disclosure documents (following Canadian rather than SEC disclosure rules) to satisfy their US registration statement disclosure requirements, as well as to satisfy continuous reporting obligations under the Exchange Act. MJDS filers are, however, also required to include in their registration statements and reports filed with the SEC any further material information necessary to make the statements in the registration statement or report not misleading.

For an offering of securities, the MJDS system generally allows the registration statement filed with the SEC to become effective immediately (except in the case of US-only offerings), and the registration statement is not subject to SEC substantive review.

In order to use MJDS, a Canadian company must be an FPI. In addition to being an FPI in order to qualify to use MJDS, a company must generally: (i) be organized under the laws of Canada (including a province or territory), (ii) not be registered or required to be registered as an "investment company" under the US Investment Company Act of 1940, as amended, (iii) have been subject to the reporting requirements of a Canadian securities regulate for at least 12 months and currently be in compliance with those requirements and (iv) have a public non-affiliate common equity float of at least US$75 million. (The exact eligibility requirements and conditions for use of any particular MJDS form are contained in the instructions to the respective form.) Offerings and sales of certain derivative securities and certain convertible securities cannot be registered under the MJDS system.

*c) Required financial statements*

**US GAAP**: If a company is not an FPI when it files a registration statement with the SEC (or when it files periodic reports with the SEC), then the company will be required to file financial statements prepared in accordance with US GAAP. As an FPI, a company is permitted to present and file its financial statements in accordance with accounting principles that are not US GAAP. The FPI must provide footnote reconciliations to US GAAP, except that an FPI whose home country GAAP (such as Canadian GAAP) is full IFRS as adopted by the IASB is not required to include any reconciliation to US GAAP. A registration statement by an issuer that is not an FPI may also be subject to the SEC's tight restrictions on use of non-GAAP financial measures, as explained in the discussion below under "Reporting and other obligations under the Exchange Act – Exchange Act reporting without FPI status."

**Date of financial statement**: Financial statements included in a registration statement and in various other documents filed with the SEC under the Securities Act or the Exchange Act must be as of a recent date. The SEC has established time frames that must be satisfied for various types of issuers:

1. For US domestic companies, including a company that is not an FPI, financial statements must generally be included in a registration statement for a date within 130 days (or 135 days for certain smaller companies) before the expected effective date of the registration statement. (Special rules determine how long and under what conditions a company can use as its latest financial statements, the unaudited statements as of the end of the most recent third fiscal quarter rather than audited year-end statements for that complete year.)

2. The staleness rules for FPIs are more favorable to the company. The last year of audited financial statements included in a registration statement filed by an FPI must generally be dated (a) within 15 months before the time of the offering or listing to which the registration statement relates, meaning the effective date of the registration statement or (b) within 12 months before the date of filing for an initial public offering, in which case the financial statements may cover a period of less than a full year. Also, if the FPI's registration statement is dated more than nine months after the end of its last audited year, the financial statements should generally include consolidated interim financial statements (which may be unaudited) covering at least the first six months of the fiscal year.

Canadian MJDS filers include in their US registration statement filings the financial statements that are required in Canada for the Canadian filing that is parallel to the US MJDS registration statement filing. The auditors of the MJDS filer's financial statements must satisfy specified US auditor independence rules and must consider whether any comments are needed for US readers as a result of reporting conflict between US and Canadian rules regarding contingencies and going concern considerations.

**Reporting currency**: FPIs are permitted to choose the reporting currency used in presenting their financial statements. If a company is not an FPI, then as a US domestic company its financial statements would have to be presented in US dollars.

**Other special financial statement requirements**: Regulation D provides companies with safe harbors to obtain a private placement exemption from registration under the Securities Act for certain securities offerings. Regulation D contains some special rules regarding the financial statements to be used and how recent they must be, with more latitude given to FPIs.

A Form S-8 registration statement under the Securities Act is used for employee benefit plans involving securities. An S-8 registration statement requires that certain financial information be delivered to employees participating in the employee benefit plan. In these requirements, FPIs are given more time to deliver year-end financial statements for the preceding year.

## Offerings outside the US; Regulation S and resale restrictions

Companies use Regulation S to provide an exemption from registration under the Securities Act for offerings and sales of securities conducted outside the US. Use of Regulation S will become more difficult and restrictive for offerings of equity securities if a company is not an FPI.

### *a) Offering restrictions under Regulation S*

Non-US companies generally rely on Regulation S to provide an exemption from registration under the Securities Act for offerings and sales of securities outside the US. Rule 901 provides that offers and sales of securities that occur outside the US are not offers and sales requiring registration or exemption under the Securities Act. Rule 903 under Regulation S sets out requirements to be followed by issuers, distributors and their respective affiliates in order for an offering and sale of securities to be viewed as occurring "outside the US" and therefore exempt from registration under the Securities Act. While Rule 903 is a safe harbor and not exclusive, the requirements of Rule 903 are the accepted standard for how an exempt offering outside the US should be conducted by the issuer, distributors and their respective affiliates, especially where there may be a risk of any US contacts.

Under Regulation S, offerings (distributions) of securities are divided into three categories:

1. A Category 1 offering is generally either:
   a. an offering of securities of an FPI that reasonably believes there is no “substantial US market interest” in its securities being offered;
      — substantial US market interest with respect to equity securities exists if (i) US exchanges constitute the single largest market for the class of securities being offered or (ii) 20 percent of trading in the class of securities being offered takes place on US exchanges and less than 55 percent of trading takes place in a single non-US country;
      — substantial US market interest with respect to debt securities exists if (i) the company’s total debt securities are held of record by 300 or more US persons or (ii) US$1 billion or more of the company’s debt securities are held of record by US persons or (iii) 20 percent or more of the company’s debt securities are held of record by US persons; or
   b. an offering of securities directed into a single non-US country to local residents where the issuer is either (i) an FPI or (ii) not an FPI and only issuing non-convertible debt not denominated in US dollars; or
   c. an offering of securities (including a grant or award) under an employee benefit plan (such as an incentive compensation plan) established and administered under the laws of a jurisdiction outside the US and using customary practices and documentation of the non-US jurisdiction, where reasonable steps are taken to prevent participation by US residents; note that US residents can participate in a simultaneous offering under the same plan if the offering to US residents is covered by a registration statement or an exemption from registration such as the Rule 701 exemption; or
   d. an offering of securities guaranteed by a non-US government.
2. A Category 2 offering is generally either:
   a. an offering of securities by an FPI that reports under the Exchange Act and is issuing equity securities; or
   b. an offering of securities by an FPI that does not report under the Exchange Act and that is issuing debt securities; or
   c. an offering of securities by a US or non-US company that reports under the Exchange Act and is issuing debt securities.
3. A Category 3 offering includes everything else, such as:
   a. an offering of equity securities where the issuer is not an FPI; or
   b. an offering of equity securities where the issuer is an FPI with substantial US market interest and does not report under the Exchange Act; or
   c. an offering of debt securities where the issuer is not an FPI and does not report under the Exchange Act.

Offerings and sales in Category 1 offerings are generally exempt from registration under the Securities Act as long as the transactions occur in “offshore transactions” without any “directed selling efforts” with respect to the US, following the offering procedures and definitions of these terms specified in Regulation S.

Offerings and sales in Category 2 offerings are generally exempt from registration under the Securities Act as long as the transactions comply with the Category 1 requirements of "offshore transactions" and no "directed selling efforts" with respect to the US plus additional offering restrictions, including a 40-day "distribution compliance period" prohibiting offers or sales of the securities to US persons during that period, plus required steps to ensure compliance with the distribution compliance period.

Offerings and sales in Category 3 offerings are generally exempt from registration under the Securities Act as long as the transactions comply with the Category 1 requirements of "offshore transactions" and no "directed selling efforts" with respect to the US plus a 40-day distribution compliance period for debt securities and a one-year distribution compliance period (six months for a company reporting under the Exchange Act) for equity securities, in each case prohibiting offers or sales of the securities to US persons during that period, plus additional required steps to ensure compliance with the distribution compliance period. These additional steps in a Category 3 offering include a legend on equity securities restricting transfer and use of a temporary global note for debt securities, in each case until the end of the distribution compliance period.

Therefore, if a non-US company does not qualify as an FPI, it will be treated like a domestic US issuer under Regulation S. That means that the equity securities it offers and sells outside the US will be subject to substantial resale restrictions as Category 3 offerings (other than securities issued under incentive compensation plans in Category 1 offerings by issuers that are not FPIs, which will be subject to separate restrictions discussed below). Those Category 3 restrictions, as described above, will include a distribution compliance period prohibiting offers or sales to or for the account of US persons for one year (or six months in the case of an issuer that reports under the Exchange Act) and restrictions to ensure compliance with this requirement. One of the principles behind Regulation S is to restrict immediate flowback into the US of securities distributed outside the US, especially by US companies, including companies organized outside the US that have so many US connections that they are no longer FPIs.

***b) Restrictions on resales outside the US if the issuer was not an FPI***

Securities issued outside the US under Regulation S can be resold by persons other than the issuer, distributors and their respective affiliates under Rule 904. (Rule 904 may also be used by officers or directors who would be deemed to be an "affiliate" only because of the individual's position as an officer or director). Resales under Rule 904 are made on non-US securities exchanges (or non-US securities markets) that are "designated offshore securities markets" designated by the SEC, and these resales must be transactions that are not pre-arranged with US purchasers. After a resale under Rule 904, the securities issued by an FPI would be cleansed of any "distribution compliance period" restriction and would generally be freely transferable (other than shares acquired in a resale by dealers or other persons receiving selling commissions if those persons are still subject to offering restrictions form the original offering).

The Toronto Stock Exchange is a "designated offshore securities market" for Rule 904 resale purposes. The other Canadian exchanges that are "designated offshore securities markets" are: the TSX Venture Exchange (an exchange generally for the securities of early-stage businesses, mostly small-cap Canadian companies), the Montreal Exchange (a derivatives exchange), the Canadian Securities Exchange (an exchange for emerging issuers) and Aequitas NEO Exchange Inc. (a new exchange established in 2015). The list of designated offshore securities market provided in Regulation S also includes the Vancouver Stock Exchange and Alberta Stock Exchange, which have both been merged into the TSX Venture Exchange.

Resales of equity securities under Rule 904 are different, however, if the issuer was not an FPI. Rule 905 provides that equity securities issued under Regulation S when the issuer is a US domestic issuer (which would include a non-US company that is not an FPI) are "restricted securities" under Rule 144. That means that those securities issued by a company that is not an FPI cannot be freely transferable under Rule 144 until the holder has held them for one year (six months for issuers that report under the Exchange Act and that have been subject to reporting for at least 90 days). During that Rule 144 holding period, the restricted securities can only be resold pursuant to a registration statement under the Securities Act or pursuant to an exemption from registration. Rule 905 specifically provides that a resale under Regulation S using Rule 904 or otherwise outside the US would not remove the transfer restriction on these "restricted securities" under Rule 144.

Therefore, these equity securities issued by a non-US company in a Category 3 offering (or under an employee benefit plan in a Category 1 offering) at a time when the issuer is not an FPI cannot be made freely transferable by sale on a non-US stock exchange. If the company were an FPI when it issued the securities, then most holders of securities (whether acquired in a Category 1, Category 2 or Category 3 offering) would be able to use the resale exemption provided by Rule 904 immediately to resell the shares publicly and allow the purchasers in those resales to acquire freely transferable shares.

Since Rule 905 provides that even a public resale under Rule 904 does not remove the "restricted" status of equity securities that were issued under Regulation S by a company that is not an FPI, transfer of such equity shares is difficult. The Toronto Stock Exchange does not have procedures to allow trading in such restricted shares through that exchange. The London Stock Exchange adopted procedures a few years ago that are intended to allow trading in restricted equity securities issued in Category 3 offerings.

Any procedures of a designated offshore securities market to allow trading in restricted securities would have to be analyzed carefully to be sure they are consistent with the requirements of Regulation S, and in any case, the resale on that system would not end the restricted nature of equity securities that had been issued under Regulation S by a non-US company when it was not an FPI. Those shares would generally remain restricted until the end of the Rule 144 oneyear (or sixmonth) holding period, unlike securities issued by an FPI, which are no longer restricted after a public resale under Rule 904.

The potential impact of Rule 905 on equity securities acquired by US and non-US directors, officers, employees and other individuals under incentive compensation plan is discussed in the next section below.

## Treatment of shares issued under incentive compensation plans

Many non-US companies issue their securities to directors, officers, employees and other persons under the company's incentive compensation plans, in issuances exempt from registration under the Securities Act. The securities acquired under these plans by US residents without registration will generally be "restricted securities." Rule 904, discussed above, provides an important resale exemption to allow US residents to resell such shares to the public, without an initial holding or waiting period, on the designated offshore securities markets designated by the SEC. But if a company is not an FPI when it issues equity securities under an incentive compensation plan in reliance on Regulation S, even the incentive compensation shares acquired by non-US residents will be "restricted securities" subject to transfer restrictions, and the availability and usefulness of Rule 904 for resales will be limited for both US residents and non-US residents, as explained further below.

***a) Issuance under incentive compensation plans without registration under the Securities Act***

A company (whether a US company or a non-US company) that is not a reporting company under the Exchange Act generally relies on Rule 701 to allow US residents to participate in its incentive compensation plans that use company securities. Rule 701 provides an exemption from registration under the Securities Act for stock-based awards (including restricted stock and stock options) to officers, directors, employees and certain other persons under incentive compensation plans where those individuals are US residents. Securities acquired by grant, vesting or exercise in reliance on Rule 701 are "restricted securities." That means that the securities acquired under those incentive compensation plans cannot be resold unless the resale of the securities is registered under the Securities Act or an exemption is available.

Individuals who are not US residents can receive their securities without SEC registration under a company's non-US incentive compensation plans in reliance on Regulation S, discussed above. Those shares issued to individuals who are not US residents are issued in "offshore transactions" and without "directed selling efforts" with respect to the US through Category 1 offerings under Regulation S, while the participation at the same time in the same plan by US residents is permitted in reliance on Rule 701. These two exemptions from registration (under Rule 701 and under Regulation S) are separate, and the two simultaneous offerings and sales are not integrated. (Note that stock awards to broad groups of employees under broad-based bonus plans (not stock option plans), where there is no direct cost to the employee and no individual agreement, may not require registration under the Securities Act on a "no-sale" theory.)

***b) Resales of shares acquired under incentive compensation plans***

Persons who are not US residents who received their incentive compensation shares under a plan established and administrated under the laws of a jurisdiction outside the US using customary local practices and documentation from a company that was at the time an FPI (where the transaction was a Category 1 offering under Regulation S) do not normally need a resale exemption since the shares they acquired would generally not be "restricted securities."

Securities acquired pursuant to an incentive compensation plan not covered by a registration statement under the Securities Act would be "restricted securities" (subject to transfer restrictions) in the following situations:

1. the securities were acquired under the plan by a US resident, whether or not the issuer was an FPI or

2. the securities were acquired by a non-US resident at a time when the issuer was not an FPI.

Rule 144 and Rule 904 offer separate and alternative exemptions from Securities Act registration for resales of "restricted securities."

Rule 144 allows restricted securities to be resold by the holder without registration under the Securities Act after a holding period of one year for an issuer that does not report under the Exchange Act (six months for issuers that report under the Exchange Act and have been subject to reporting for at least 90 days). Sales by affiliates (including executive officers and directors) are also subject to additional restrictions under Rule 144 (availability of current information and limits on amounts sold).

Rule 904, discussed above, provides an important alternative resale exemption for restricted securities. Unless the officers, directors, employees and other persons are deemed to be "affiliates" of the issuer (other than merely because of a position as an officer or director), they can have immediate liquidity for their shares using Rule 904. As mentioned above, Rule 904 allows immediate resale of such securities of an FPI on a "designated offshore securities market" in transactions that are not pre-arranged with US purchasers. (With respect to resales by officers or directors of the issuer using Rule 904, there is also the requirement that no fees can be paid for the resale beyond customary broker's commissions.)

If a company had been an FPI but lost its FPI status:

1. Rule 904 and the immediate public liquidity it provides to shareholders (without any holding period or waiting period) would remain available to current and former officers, directors, employees and other individuals to allow immediate resale on a designated offshore securities market of the equity securities of the company that had been acquired (by vesting, grant or exercise of stock options) at a time when the company was an FPI under the company's incentive compensation plans; after use of Rule 904 for the resale, such securities would generally be cleansed of restrictions and would be like other freely transferable securities acquired on such offshore exchange.

   **but**

2. Equity securities acquired (whether by US residents or by non-US residents) under incentive compensation plans at a time when the company was not an FPI would be "restricted securities" under Rule 144 as provided in Rule 905, and until the end of the one-year or six-month holding period under Rule 144, those securities could only be resold under a registration statement under the Securities Act or under an exemption from registration; any transfer pursuant to an exemption before expiration of the holding period would not remove the "restricted" status so the securities would remain "restricted" even after a Rule 904 resale, making a public resale difficult given current market practices.

That means that all holders of securities acquired under incentive compensation plans in reliance on Rule 701 or Regulation S when the issuer was not an FPI, including not only US residents but also residents of any other jurisdiction, will generally only be able to resell those securities in the public markets: (a) after satisfying the minimum holding period of one year or six months, as applicable, under Rule 144, (b) by selling under a registration statement filed by the issuer covering the resale or (c) by selling on a designated offshore securities market that will retain the restricted status of the shares after resale using procedures satisfying Regulation S.

The offer, sale and resale of the interests and securities under a company's incentive compensation plans can be registered under the Securities Act using a simple Form S-8 registration statement. That registration generally allows the securities to be freely transferable without a holding period. The simple S8 registration statement form, however, may only be used if a company is subject to the reporting requirements under the Exchange Act.

## Communications during an offering

The Securities Act restricts public communications (interpreted broadly) in any form during, or in connection with, an offering of securities where those communications may arouse interest in a company or its securities, whether or not an offering is mentioned. Beyond the formal prospectus contained in a company's Securities Act registration statement, a company is permitted by various rules to make certain specific types of communications subject to specified conditions. Some of these rules provide more accommodations to FPIs than to companies that are not FPIs when making statements and providing information during or relating to an offering of securities where the communications may enter the US. Specifically:

- Rule 135e generally allows FPIs to issue press releases outside the US, hold press conferences outside the US and have meetings with journalists outside the US in connection with an offering (other than an offering conducted solely in the US) without triggering any requirement to file a registration statement or the communication under the Securities Act, even if US journalists and US media have certain access to the information. Those press releases, press conferences and meetings may contain communications, accompanied by certain required legends, that can provide information that non-FPIs would be prohibited from providing (such as the names of underwriters). Rule 135e is sometimes relied upon by FPIs for offerings conducted only in countries outside the US.

- Rule 168 provides certain larger more established FPIs (and FPIs that report under the Exchange Act) with protection when releasing routine factual business information and forward-looking information during an offering of securities. Those protections are better than similar but narrower provisions contained in Rule 169 that would apply to companies that are not FPIs and do not report under the Exchange Act.

- Rules 137, 138 and 139 contain certain conditions that permit broker-dealers to issue and distribute research reports about a company and its securities during an offering of securities by that company. Rules 138 and 139 are somewhat less restrictive and more favorable if that company is an FPI.

## Reporting and other obligations under the Exchange Act

Compliance with continuing reporting requirements under the Exchange Act after SEC registration is generally easier and costs less if the non-US company qualifies as an FPI.

If a company registers securities under the Exchange Act (which will be required if it lists securities on the NYSE or NASDAQ), then the company will want to be an FPI so that:

1. the company is not subject to the US proxy rules or the US insider trading and reporting rules under the Exchange Act and

2. the company is not subject to certain provisions of the US Sarbanes-Oxley Act of 2002, as amended (**Sarbanes-Oxley**), the US Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, as amended (**Dodd-Frank**) and related rules.

Note that "registration" under the Exchange Act, "reporting" under the Exchange Act and "listing" on a US stock exchange under the Exchange Act each has specific consequences, which are sometimes overlapping and sometimes different.

Note also that companies that are required to file reports with the SEC may not be treated the same in certain respects as companies that voluntarily report to the SEC (which may happen if the company's creditors require that the company file those reports). In this document, whenever we refer to a company that "reports" or is "reporting" under the Exchange Act, we assume it is reporting because it is required to report by the provisions of the Exchange Act.

***a) Circumstances under which a company is required to report under the Exchange Act***

A company will generally be required to report under the Exchange Act if any one of the following three triggers occurs, each of which could be applicable regardless of whether an issuer is an FPI or treated as a US domestic company (but if registration would otherwise be required due to the third trigger below, a valuable exemption is available to FPIs):

1. A company registers a public offering of its securities (whether debt or equity) under the Securities Act; this registration under the Securities Act triggers reporting for some period under the Exchange Act, but there is no "registration" under the Exchange Act; or

2. A company lists securities on a US stock exchange such as the NYSE or NASDAQ; this would require registration of the class of listed securities under Section 12(b) of the Exchange Act, which would trigger reporting; or

3. (a) A company (with assets of more than US$10 million) has global record holders of a class of its equity securities (counting registered holders and the participants on a depository and clearing trading system such as DTC or CDS, but not their underlying beneficial accounts for this purpose) that either (i) reach a total number of 2,000 or more record holders or (ii) for entities that are not a bank, a savings and loan holding company or a bank holding company, include 500 or more record holders who are not "accredited investors" (as defined in the Securities Act); this is tested as of the end of the company's fiscal year, and this determination of record holders does not drill down to customer accounts of nominees as is done when looking at US share ownership for FPI purposes; securities that were acquired under incentive compensation plans in transactions that were not required to be registered under the Securities Act are generally excluded in making these determinations; and

   (b) 300 or more of the beneficial owners of that class of equity securities (drilling down to look at underlying customer accounts) are resident in the US;

   such a class of securities reaching the thresholds of clauses (a) and (b) of this third trigger must be registered under Section 12(g) of the Exchange Act, which triggers reporting.

Regardless of their numbers of record and US beneficial holders, FPIs can use Exchange Act Rule 12g3-2(b), which provides FPIs with an exemption from registration under the Exchange Act that would otherwise be required because of trigger 3 above. In order to use the Rule 12g3-2(b) exemption, the FPI must meet certain conditions including: (1) the company must publish in English on its website or on an electronic information delivery system generally available to the public in its primary trading market (such as SEDAR in Canada), the information the company (a) has made public or been required to make public under the laws of the country of its incorporation, organization or domicile, (b) has filed or been required to file with its principal stock exchange in its primary trading market and that has been made public by that exchange and (c) has distributed or been required to distribute to holders of its securities and (2) the primary trading market for such equity securities must be outside the US, meaning that at least 55 percent of average daily global trading in the most recent fiscal year took place on facilities of securities markets in (i) one non-US jurisdiction or (ii) two non-US jurisdictions (with one of those two having more trading than in the US).

(A company could voluntarily register a class of securities under Section 12 (g) of the Exchange Act, which would then require the company to file reports under the Exchange Act. A company could do that if it wanted to have trading in those securities quoted on the OTC Bulletin Board to facilitate US over-the-counter trading.)

***b) Exchange Act reporting without FPI status***
**Reporting forms for non-FPI**: If a company is required to file periodic reports under the Exchange Act (such as after a listing on the NYSE or NASDAQ) and is not an FPI, then it would be required to file with the SEC using the forms for a US domestic company, including: (i) current reports on Form 8-K, (ii) quarterly reports for the first three quarters on Form 10-Q (including unaudited quarterly financial statements and a related Management's Discussion and Analysis) and (iii) annual reports on Form 10-K, all of which are forms for US domestic companies and use full SEC disclosure rules for US domestic issuers, including greater compensation disclosure compared to what FPIs normally provide.

**FPI reporting forms**: FPIs that have securities registered under the Exchange Act (i) can generally "furnish" current reports and quarterly reports on Form 6-K (using home country disclosure rules) and (ii) can "file" annual reports on Form 20-F (using SEC disclosure rules modified somewhat for non-US companies) or for Canadian MJDS filers, on Form 40-F (using Canadian disclosure rules). The US annual report (a Form 40-F) for Canadian FPI MJDS filers is primarily a wrap around the company's Annual Information Form, annual Management's Discussion and Analysis and annual Audited Financial Statements, each as filed in Canada, together with certain Sarbanes-Oxley and Dodd-Frank certifications and disclosures. In filing annual reports with the SEC, FPIs have a later deadline (up to four months after fiscal year-end) than companies that are not FPIs; Canadian FPIs that are MJDS filers, file their annual report with the SEC on the same day that they file in Canada. (Information that is "furnished" by FPIs, as opposed to being "filed," may be subject to less potential liability under the Exchange Act. Reports "furnished" to the SEC will be deemed "filed" if they are incorporated into a registration statement. Whether an item is furnished or filed with the SEC, it will generally appear on the publicly accessible EDGAR system. In this document, when we refer to "filed" we generally are referring to items provided to the SEC and are not distinguishing between items that are "furnished" versus "filed.")

**Actions requiring current reports (6-K vs. 8-K)**: An FPI furnishes to the SEC on Form 6-K a copy of any information the company: (1) makes public or is required to make public under the laws of the jurisdiction of its incorporation, organization or domicile, (2) files or is required to file with a stock exchange on which its securities are traded and that has been made public by that exchange or (3) distributes or is required to distribute to holders of its securities. If a non-US reporting company is not an FPI and therefore is required to file under the Exchange Act as a US domestic company, the company would instead be required to make current disclosures concerning many specified events in a Form 8-K filed with the SEC. Form 8-K is more structured than a Form 6-K, identifying events that require current disclosure and requiring specific information regarding those events.

**Quarterly reports**: An FPI is not required to furnish quarterly reports to the SEC unless it makes them publicly available outside the United States. If a non-US reporting company is not an FPI and therefore is required to file under the Exchange Act as a US domestic company, the company would be required to file quarterly reports on Form 10-Q (using SEC disclosure rules), including unaudited financial statements and a US form of management's discussion and analysis, with respect to each of its first, second and third fiscal quarters each year. (The NYSE and NASDAQ require listed FPIs to file unaudited semi-annual financial statements covering the first two fiscal quarters.)

**Quarterly assessments and certifications**: In addition, US domestic reporting companies (including a non-US company that is not an FPI) that report under the Exchange Act are obligated, on a quarterly basis, to assess changes in their internal control over financial reporting and evaluate the effectiveness of disclosure controls and procedures, and their quarterly Form 10-Q must be accompanied by certifications (including certifications regarding financial statements, disclosure controls and procedures and internal control over financial reporting) from the principal executive officer(s) and principal financial officer(s) pursuant to Sections 302 and 906 of Sarbanes-Oxley. For an FPI, these assessments, evaluations and certifications are required only in its annual report on Form 20-F (or Form 40-F for a Canadian MJDS filer). On an annual basis, FPIs and US domestic companies that report under the Exchange Act are required to submit assessments of the effectiveness of their internal control over financial reporting, and the auditors of the company's annual financial statements must issue an attestation report regarding management's assessment of the effectiveness of internal control over financial reporting. Certain accommodations are provided for this assessment and attestation for new reporting companies and for "emerging growth companies."

**Non-GAAP financial measures**: If a reporting company is not an FPI, it would also have to comply with the requirements of Regulation G regarding use of non-GAAP financial measures (whether in writing or orally) in SEC filings (such as registration statements and required reports) and in other public disclosures in the US. Regulation G requires that use of a non-GAAP financial measure must be accompanied by disclosure of the most directly comparable GAAP measure and a reconciliation between the non-GAAP measure and such GAAP measure. As applied by the SEC staff, Regulation G (with its broad prohibition on using a non-GAAP financial measure in a misleading way) prohibits many specific formulations and presentations of non-GAAP financial measures and is more restrictive in certain respects than, for example, the comparable Canadian restrictions. A company is generally not subject to Regulation G as long as (1) it is an FPI whose securities are listed or quoted on an exchange or quotation system outside the US, (2) the non-GAAP financial measure is not based on a US GAAP measure and (3) the disclosure of the non-GAAP financial measure in the US is also made outside the US (and not targeted at persons in the US). Regulation G generally does not apply to filings by a Canadian FPI on MJDS forms. The principles behind Regulation G may, however, still apply to filings by an FPI to the extent the SEC staff views the use of a non-GAAP financial measure as potentially misleading.

**Financial statements** As discussed above under "Registration under the Securities Act or under the Exchange Act," if a company is not an FPI, its financial statements contained in SEC filings would have to be prepared in accordance with US GAAP. Also see the related discussions above regarding reporting currency and staleness of financial statements in SEC filings.

***c) Other significant consequences of having securities registered under the Exchange Act and not being an FPI***

In addition to the differences noted above in reporting requirements for an FPI versus a US domestic company, there are other significant consequences under the Exchange Act for a non-US company that loses FPI status. If a company has a class of securities registered under the Exchange Act at a time when the company is not an FPI, the company would become subject to the following significant consequences applicable to US domestic companies whose securities are registered under the Exchange Act:

- *US proxy rules*: The company would become subject to the US proxy rules with respect to the class of registered securities. These rules regulate proxy solicitation (disclosure and procedures) and regulate the annual meeting process. FPIs are not subject to the US proxy rules.

- *Section 16 insider trading reports*: For companies (other than FPIs) with a class of equity securities that is registered under the Exchange Act, the officers, directors and shareholders holding more than 10 percent of the registered class of equity securities are required to file reports of beneficial ownership of the company's equity securities under Section 16(a) of the Exchange Act. These insiders will be required to file reports with the SEC (Forms 3, 4 and 5) regarding their non-exempt purchases and sales of the company's common shares, options and other derivative securities. These requirements will not apply if the company is an FPI.

- *Section 16 short-swing profit recovery*: For companies (other than FPIs) with a class of equity securities registered under the Exchange Act, the officers, directors and shareholders holding more than 10 percent of the registered class of equity securities are subject to the short-swing profit recovery rules under Section 16(b) of the Exchange Act. These rules require that these insiders disgorge to the company, on a strict liability basis, any profits from matching non-exempt purchases and sales of the company's equity securities made within any six-month period. These rules will not apply if the company is an FPI. (Section 16(c) prohibits these same persons from (1) selling any equity securities of the company when the person does not own the security or (2) failing to deliver the security after it is sold within certain time frames in certain situations. These short sale prohibitions do not apply if the company is an FPI.)

- *Sarbanes-Oxley and Dodd-Frank*: Certain requirements of Sarbanes-Oxley, Dodd-Frank and related rules that apply to a company that has securities registered under the Exchange Act either do not apply to FPIs or treat FPIs more favorably. Some of these provisions are listed below:

- *"Say-on-pay" vote*: A company is required to conduct advisory shareholder votes at least once every three years regarding the compensation of its top executive officers. At least once every six years, the company must conduct a shareholder vote on the frequency of these advisory votes. An advisory shareholder vote is also required regarding executive golden parachute compensation in connection with an acquisition or disposition transaction. These requirements do not apply to FPIs.

- *Pay ratio disclosure*: A company must disclose the ratio of its annual total CEO compensation compared to the median annual salary of all of its employees. This applies not only to a company that has securities registered under the Exchange Act but also to a company that is just reporting under the Exchange Act. This requirement does not apply to FPIs.

- *Pay vs. performance disclosure*: A company must disclose a comparison of the CEO's total compensation and the average total compensation of the executive officers against the company's total shareholder return and must compare the company's total shareholder return against the return for a peer group. (A rule containing these requirements has been proposed but has not yet been adopted. The requirements as proposed would not apply to FPIs.)

- *Independent audit committee; observer*: Companies that have securities listed on a US stock exchange (such as the NYSE or NASDAQ) must have audit committees composed only of independent board members. But an FPI is also permitted to have one audit committee member that is an affiliate of the FPI if the individual is not an executive officer, only has observer status and is not a voting member or chair of the audit committee. Certain further exceptions to the independence requirement are available to FPIs in certain specific situations.

- *Independent compensation committee*: Companies that have securities listed on a US stock exchange (such as the NYSE or NASDAQ) must have compensation committees composed only of independent board members (or in limited circumstances, NASDAQ permits a committee of at least three members to have one member who does not meet the independence requirements). The SEC leaves to the board the ultimate determination as to the independence of compensation committee members. FPIs that disclose in their annual report the reasons why they do not have an independent compensation committee are exempt from the compensation committee independence requirements. (The independent compensation committee requirements also do not apply to a "controlled" company, which is a company that has an individual, entity or group holding more than 50 percent of the power to elect directors.)

- *Hedging policy*: Starting with fiscal years beginning on or after July 1, 2019, companies will be required to disclose whether employees (including officers) or directors or their designees are permitted to purchase financial instruments, or otherwise engage in transactions, that hedge or offset, or are designed to hedge or offset, any decrease in the market value of a company's equity securities granted to the employee or director as compensation or otherwise held directly or indirectly by the employee or director. This requirement does not apply to FPIs.

- *Trading during pension fund trading blackouts*: During certain trading blackouts for participants in ERISA "individual account plans," directors and executive officers of a company that has securities registered, or that reports, under the Exchange Act are generally prohibited by Regulation BTR under the Exchange Act from trading in any equity or derivative security of the company where the security was acquired in connection with service or employment as a director or executive officer. This applies not only to a company that has securities registered under the Exchange Act but also to a company that is just reporting under the Exchange Act. But the directors and executive officers of an FPI are not covered by this restriction unless (1) 50 percent or more of the participants or beneficiaries located in the United States in individual account plans maintained by the company are subject to the temporary trading suspension and (2) the affected US participants and beneficiaries represent an appreciable portion (as defined) of the company's worldwide employees.

- *Disclosure of material non-public information:* If a company has securities registered, or reports, under the Exchange Act and is not an FPI, it would become directly subject to US Regulation FD. Regulation FD prohibits selective disclosure and generally provides that when a company discloses material non-public information to certain persons (including securities analysts, other securities market professionals and holders of the company's securities who could reasonably be expected to trade on the basis of the information), the company must make simultaneous public disclosure of that information (in the case of intentional disclosure) or prompt public disclosure (in the case of non-intentional disclosure). FPIs are technically exempt from Regulation FD, but they are subject to Section 10(b) under the Exchange Act which imposes requirements similar to Regulation FD.

- *XBRL data tagging*: If a company that has securities registered or that reports under the Exchange Act files financial statements with the SEC using US GAAP or IFRS as issued by the IASB (which is Canadian GAAP), then those financial statements must generally be presented in XBRL format and comply with the XBRL data tagging rules. Certain accommodations exempt FPIs from XBRL tagging for most quarterly financial statements.

Please note that this section and the following section do not list every requirement, restriction and condition imposed on entities as a consequence of having a class of securities registered, or being required to report, under the Exchange Act.

***d) Certain consequences of Exchange Act registration applicable to all issuers (whether or not an FPI)***

In addition to the consequences discussed above arising from Exchange Act registration (or in some cases, reporting) without FPI status, note that all companies (including FPIs) that have securities registered under the Exchange Act (such as in the case of a listing of shares on the NYSE or NASDAQ) are subject to the rules listed below. A company would also become subject to some of these rules if it were required to report under the Exchange Act solely as a result of having filed a registration statement for an offering and sale of securities under the Securities Act.

- *Beneficial ownership reporting*: Sections 13(d) and 13(g) of the Exchange Act impose disclosure obligations (filing of a Schedule 13D or 13G) on persons who acquire beneficial ownership of more than 5 percent (individually or as part of a group) of a class of voting equity securities that is registered under the Exchange Act.

- *US tender offer Rules*: A tender offer or takeover bid that has sufficient US contacts can be subject to US tender offer rules. Section 14(e) of the Exchange Act contains tender offer rules for unregistered debt or unregistered equity securities. A tender offer for securities that are registered under the Exchange Act is generally subject to the more detailed rules under Section 14(d) governing disclosures, filings, procedures and terms and conditions of the tender offer.

- *Sarbanes-Oxley and Dodd-Frank*: The following requirements of Sarbanes-Oxley, Dodd-Frank and related rules are applicable to a company that has securities registered under the Exchange Act, whether or not the company is an FPI:

  — *Auditor independence and pre-approval*: The company's auditors are required to be independent and the company's audit committee must pre-approve audit and non-audit services provided by the auditors. This applies if the company has securities registered, or just reports, under the Exchange Act.

  — *Compensation committee consultants*: The compensation committee of a company that has securities listed on a US stock exchange may, in the committee's sole discretion, retain or obtain the advice of compensation consultants and other advisers, but before doing that, the committee must consider specified independence factors, and companies must provide funding for the retention of these advisers. Compensation committees are directly responsible for the selection, compensation and oversight of the advisers they retain. FPIs are not exempt from these compensation adviser requirements.

- *Clawback*: A company's CEO and CFO could be subject to disgorgement of certain profits and bonuses if there is an accounting restatement of the company's financial statements due to material non-compliance with any financial reporting requirement under US securities laws that occurred as a result of misconduct. An expanded Dodd-Frank rule for companies that have securities listed on a US stock exchange has been proposed but not yet adopted. The proposed expanded requirement would apply if there is an accounting restatement due to material non-compliance with a financial reporting requirement (regardless of whether there was any misconduct) and would provide for mandatory recovery from executive officers of any incentive based compensation those executive officers should not have received after giving effect to the restatement.

- *Prohibition on loans*: A company that has securities registered, or just reports, under the Exchange Act is prohibited from making loans or extensions of credit to the company's directors and executive officers.

- *Whistleblower protections*: Sarbanes-Oxley provides that a company that has securities registered, or just reports, under the Exchange Act is prohibited from retaliating against whistleblowers; Dodd-Frank expanded these whistleblower protections in certain situations and provides for bounties to whistleblowers.

- *Internal control over financial reporting and disclosure controls and procedures*: Companies that have securities registered, or just report, under the Exchange Act are required to maintain (1) subject to a transition period, a process for internal control over financial reporting designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements under GAAP and (2) disclosure controls and procedures designed to ensure that information required to be reported to the SEC under the Exchange Act is properly recorded, gathered, reviewed and reported in a timely manner.

- *Certain disclosures*: Various disclosures are required regarding: (i) a code of ethics for senior executives and any waivers that have been granted, (ii) off-balance sheet arrangements, (iii) the identity of audit committee members for companies listed on a US stock exchange, (iv) contractual obligations, (v) whether an "audit committee financial expert" sits on the audit committee of the company's board, (vi) fees and services of the principal accountants auditing the company's financial statements, (vii) use of any "conflict minerals" (originating in the Democratic Republic of the Congo or an adjoining country) that are necessary for the functionality or production of a product manufactured by the company or contracted by the company to be manufactured, (viii) for issuers engaged in the commercial development of oil, natural gas or mineral resources, certain payments to the US federal government or to a non-US government (but currently there is no rule in effect to enforce this requirement of Dodd-Frank), (ix) mine safety and regulatory compliance for issuers operating coal or other mines, and (x) certain Iran-related activities.

• *Foreign Corrupt Practices Act*: If a company is required to report under the Exchange Act (whether as a result of registration under the Exchange Act or registration under the Securities Act), it is subject to the US Foreign Corrupt Practices Act, which contains various provisions regarding accounting, books and records and internal control, as well as anti-bribery provisions.

• *SEC review of annual filings*: Sarbanes-Oxley requires the SEC to review the annual filing under the Exchange Act (on Form 10-K, 20-F or 40-F) of each company that has securities listed on a US stock exchange (whether or not the company is an FPI) at least once every three years. The SEC, however, has extended this review to every company reporting under the Exchange Act, whether or not its securities are listed on a US stock exchange. For a Canadian FPI that qualifies as an MJDS filer, this SEC review of annual filings could generally include, among other things: (i) reviewing compliance with IFRS requirements, (ii) asking the company for support for statements that appear to be overly aggressive, not sufficiently supported, incomplete or inconsistent (such as the value of an asset or an assumption about a future outcome) or (iii) criticizing extensive or prominent use of non-GAAP financial measures. Typically, either the SEC is satisfied with the company's responses made in correspondence with the SEC or the company agrees that the challenged disclosure will not be repeated or will be corrected in future filings (generally without amending the filings that were reviewed).

## Cross-border acquisitions; dealing with US shareholders

An acquisition might be structured as a tender offer or takeover bid, where the target shareholders are offered securities (an exchange offer) or cash, or as a merger, amalgamation or other form of business combination. If a non-US company acquires or combines with another non-US company, there may be US resident shareholders of the target company or of both companies.

The Securities Act is generally relevant if:

1. securities of the acquiror are offered to US resident shareholders of the target company or
2. securities of a new successor entity are offered to US resident shareholders of either company.

An "offer" of securities under the Securities Act can be a direct exchange offer or may be the solicitation of a vote that will result in the securities being received.

The US tender offer rules under the Exchange Act are generally relevant if a tender offer or takeover bid is made or extended to US residents.

The rules and forms under the Securities Act and under the Exchange Act provide various exemptions and accommodations for acquisitions and combinations involving FPIs.

***a) Securities Act registration of shares***

A registration statement under the Securities Act will be required in connection with the offer and issuance of new shares to be issued by the acquiror or by the combined entity unless an exemption from registration is available.

Companies may sometimes be able to structure the transaction as a court-approved transaction satisfying the requirements of the exemption provided by Section 3(a)(10) of the Securities Act, which for Canadian companies would mean structuring the transaction as a plan of arrangement.

For acquisitions that do not meet the conditions of Section 3(a)(10), Rule 802 provides an important exemption from registration under the Securities Act. Rule 802 generally provides an exemption from registration if any company whose securities will be exchanged for securities of the acquiror or for securities of a successor company is an FPI and:

1. US residents beneficially hold no more than 10 percent of the class of securities that are to be acquired from shareholders of the subject FPI in the case of either (a) a takeover (exchange) offer or (b) an amalgamation (business combination) where the subject FPI's shares are acquired using the acquiror's securities or
2. US residents will beneficially hold no more than 10 percent of the class of new securities of the new combined company immediately after the combination in the case of an amalgamation (business combination) where shareholders of the two FPIs receive the new company's securities.

The above conditions under Rule 802 regarding the percentage of US resident shareholders generally do not apply if the exchange offer or business combination is commenced while a prior exchange offer or business combination is pending that is relying on Rule 802. There are further conditions to the use of Rule 802, including that the transaction information documents include specified legends and that those information documents be furnished to the SEC, as well as other requirements and details.

If Rule 802 is not available to provide an exemption from SEC registration, Canadian companies that are eligible to use the MJDS system may be able to use one of the MJDS registration statement forms (Forms F-8, F-80 or F-10) for shares issued in the acquisition. The choice between the forms will depend mainly on the percentage of shares held of record by US residents. Use of any of these forms is subject to certain conditions and compliance with certain requirements. These MJDS forms are basically wraps around the Canadian information documents or circulars used in the acquisition (which are prepared under Canadian disclosure rules), and SEC registration on Form F-8 or F-80 does not trigger further SEC reporting obligations after the deal is completed.

There are special rules and presumptions for determining the percentage of shares beneficially owned by US residents for purposes of applying the Rule 802 exemption and to determine the percentage of shares held of record by US residents for purposes of qualifying to use the different MJDS registration statement forms in an acquisition or combination.

(Rule 801 deals in a similar way with rights offerings, where a company gives holders of an existing class of its equity securities the right to acquire more of the same securities. Rule 801 exempts a rights offering by an FPI from registration under the Securities Act in situations where not more than 10 percent of the class of equity securities that is the subject of the rights offering is currently held by US resident shareholders, subject to certain requirements.)

***b) Tender offer rules***

If a transaction is structured as a tender offer or takeover bid that extends to or is made to US resident shareholders, the US tender offer rules may apply under Section 14(d) of the Exchange Act (for target securities registered under the Exchange Act) or under Section 14(e) of the Exchange Act (for securities not registered under the Exchange Act). Rule 14d-1 under the Exchange Act provides important exemptions from most of the Exchange Act tender offer rules (regarding the conduct and terms of the tender offer) for:

1. a tender offer conducted under Canadian law where the target company is a Canadian FPI and less than 40 percent of the target class of securities is held by US residents or

2. a tender offer where the target company is an FPI (from any country) and not more than 10 percent of the target class of securities is held by US residents (referred to as the Tier I exemption); a bidder can use the Tier I exemption without regard to the 10 percent test if there is already another pending tender offer relying on the Tier I exemption.

Where target FPIs do not qualify under (1) or (2) above, Rule 14d-1 provides that the bidder can still be relieved from some of the tender offer requirements if not more than 40 percent off the target class of securities is held by US residents (referred to as the Tier II exemption). A bidder can use the Tier II exemption without regard to the 40 percent test if there is already another pending tender offer relying on the Tier II exemption.

There are special rules and presumptions for determining US resident shareholdings for these exemptions from the US tender offer rules, and these exemptions are subject to certain further conditions.

Rule 14d-1 also provides certain exceptions from the tender offer communication rules for a press release, press conference or meeting with journalists where the release, conference or meeting occurs outside the US and relates to a target company that is an FPI, subject to satisfying certain conditions.

Similar exemptions from tender offer rules are available to FPIs that conduct self-tenders going after their own securities.

## Listing on a US stock exchange

FPIs that have securities listed on a US stock exchange, such as the NYSE or NASDAQ, are given various accommodations under US stock exchange rules (which are approved by the SEC). FPIs may follow "home country practices" in lieu of certain corporate governance requirements otherwise imposed by the US stock exchange (including shareholder approval requirements) but must generally disclose in their annual reports on Form 20-F (or 40-F for a Canadian MJDS filer) each NYSE or NASDAQ requirement that they do not follow. The NYSE also requires that the FPI describe the significant differences in its alternative practices compared to the required practices for US domestic companies. NASDAQ requires a description of the home country practices but does not expressly require disclosing the significant differences.

This accommodation for home country practices is not available to a company that has securities listed on the NYSE or NASDAQ and is not an FPI. FPIs whose securities are listed in the US have decided either to take advantage of this home country governance exemption or instead have followed some or all of the practices applicable to a US company, based in part on what their peers are doing.

Some of the NYSE and NASDAQ rules that allow FPIs to follow home country practices rather than the rules for a US domestic company include rules on the following corporate governance matters (and a "controlled" company, where an individual, entity or group holds more than 50 percent of the power to elect directors is also exempted from some of these provisions):

- Majority of independent directors;
- US definition of "independence";
- Regular meetings of non-management board members or of independent board members;
- Independent nominating/corporate governance committee;
- Independent compensation committee; and
- Shareholder approval of equity compensation plans and of certain material transactions.

## Transition if FPI status is lost

If a company that had previously determined that it qualified as an FPI determines that it no longer qualifies as an FPI, then if the company is reporting under the Exchange Act or has an active registration statement on file under the Securities Act, the company must transition to status as a US domestic company. The company would become subject to the registration statement and reporting requirements under the Securities Act and Exchange Act applicable to a US domestic company beginning on the first day of the next fiscal year. Such a company would generally continue to be eligible to use the forms for FPIs for registration and reporting with the SEC until the end of its fiscal year but would lose that eligibility as of the first day of its next fiscal year. Canadian MJDS filers who lose FPI status would, however, immediately lose the ability to use MJDS Securities Act registration forms.

If an issuer that reports under the Exchange Act no longer meets the definition of an FPI because it incorporates in a state, territory or possession of the United States, then it must immediately begin filing reports under the Exchange Act as a US domestic company.

The NYSE generally provides for a six-month transition period for most of its FPI accommodations when a company loses FPI status. NASDAQ does not specify a transition period in its rules.

In the case of any loss of FPI status, the exact consequences and the timing of the transition need to be considered carefully under the precise circumstances.

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Again, the above is a summary. There may be additional relevant details depending on the precise circumstances.

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## Norton Rose Fulbright

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