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Recent Developments in International Securities Regulation

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I. INTRODUCTION

The defining characteristic of modern securities markets is that they are organized and regulated primarily on a national basis.[1] Yet in the past ten to fifteen years international offerings of securities, international trading and the cross-border provision of financial services have increased dramatically.[2] The development of international securities regulation is in large part a reaction to these related market developments. There are three principal facets of the internationaliza-

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1. *See* Securities and Investment Board, *Regulation of the United Kingdom Equity Markets: Discussion Paper*, Feb. 1994, at 1, 7.

2. E.g., Griffiths, *Trends in International Equity Issuance*, *in* GLOBAL OFFERINGS OF SECURITIES: ACCESS TO WORLD EQUITY CAPITAL MARKETS (M. Brown and A. Paley, eds. 1994) [hereinafter Brown and Paley] ("[b]y the end of 1993 we saw the emergence of a new, global capital market overlying the long-established domestic markets"); see also Breeden, *Reconciling National and International Concerns in the Regulation of Global Capital Markets*, *in* the INTERNATIONALIZATION OF CAPITAL MARKETS AND THE REGULATORY RESPONSE 27 (Fingelton ed. 1992) [hereinafter Fingelton]; Neuberger, LSE Financial Markets Group, Special Paper No. 33 (unpublished paper from Conference on European Financial Markets, London Oct. 1990) [hereinafter Capital Markets] ("[w]ith wider economic integration, the notion of largely national markets which trade shares in domestic companies between institutions and individuals which are based domestically must be coming to an end").

tion of securities regulation. First, national securities regulation, by dealing more frequently and directly with international issues, has taken on an increasingly international dimension. Thus, for example, the United States Securities and Exchange Commission ("SEC" or "Commission") adopted an integrated disclosure system for foreign private issuers in the 1980s and expanded it in the 1990s.[3] Second, national securities regulators have expanded significantly cooperative efforts to address, both bilaterally and multilaterally, international securities problems. For example, in 1991 Canada and the United States adopted amendments to their own national regulations designed to accommodate and facilitate increased securities transactions between the two countries.[4] Third, several regional or international institutions, the most successful being the European Union ("EU"), are attempting to develop (in the case of the EU, has developed) regulatory responses to the internationalization of the world's securities markets.[5] Despite a significant increase in international efforts to regulate world securities markets, however, at present securities regulation is still primarily carried out on a national basis.[6]

The discussion of emerging trends in international securities regulation necessarily begins with a review of data concerning the interdependence of the world's securities markets. Foreign private issuers filed registration statements with the SEC in 1993 covering approximately $46 billion of securities.[7] According to some estimates, in 1993 foreign issuers also privately placed over $50 billion of securities in the United States, including approximately $24.5 billion of securities in "Rule 144A placements."[8] For the period July 1991 through December 1993, 50 Canadian issuers filed 70 registration statements, covering

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3. Adoption of Foreign Integrated Disclosure System, Sec. Act Rel. No. 33-6437, [1982 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 72,407 (Nov. 19, 1982); Simplification of Registration and Reporting Requirements for Foreign Companies; Safe Harbors for Public Announcements of Unregistered Offerings and Broker-Dealer Research Reports, Sec. Act Rel. No. 33-7053, [1994 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,331 (Apr. 19, 1994).

4. Multijurisdictional Disclosure and Modifications to the Current Registration System for Canadian Issuers, Sec. Act. Rel. No. 33-6902, [1994 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,812 (June 21, 1991); Multijurisdictional Disclosure System, National Policy Statement No. 45, Can. Sec. L. Rep. (CCH) ¶ 4,250.

5. *E.g.*, Warren, *Global Harmonization of Securities Laws: The Achievement of the European Communities*, 31 HARV. INT'L L. J. 185 (1990).

6. *See* Goodhart, *The Crash of October 1987*, LSE Financial Markets Group, Special Paper No. 06, at 5 (unpublished manuscript) (on file with author) (that banking systems and capital markets have close interrelationships is "clear beyond peradventure").

7. UNITED STATES SECURITIES AND EXCHANGE COMMISSION, 1993 ANNUAL REPORT 51 (1994) [hereinafter SEC 1993 ANNUAL REPORT].

8. Tom Kershaw, *Scouring the Globe for the Traditional Private Market*, INVESTMENT DEALERS' DIG., Mar. 7, 1994, at 16. Both the private placement and 144A figures reported are under-inclusive in the sense that they reflect only transactions conducted by or through a placement agent.

over $11 billion of securities, pursuant to the U.S. Multijurisdictional Disclosure System ("MJDS").[9] At the end of 1993, there were 588 foreign companies from 40 countries filing reports with the Commission.[10]

In 1993, domestic registrants filed registration statements covering approximately $822 billion of securities,[11] some portion of which was sold offshore. For the period November 1992 through the end of 1993, 97 issuers filed unallocated shelf registration statements with the SEC covering $73.1 billion of securities.[12] During 1993, U.S. issuers reportedly sold approximately $123 billion of securities in private placements, including $66.8 billion of securities sold in Rule 144A placements.[13] U.S. issuers borrowed $24.8 billion on international and foreign bond markets in 1993,[14] Eurodollar offerings accounting for $16.1 billion of this amount.[15] In the same year U.S. companies issued $9.9 billion of international equities,[16] some pursuant to registration and some pursuant to SEC Regulation S. "Hundreds of U.S. equities are traded on foreign stock exchanges by the larger U.S., Japanese, and European broker-dealers, which have established trading desks at the major markets around the world.[17]

The SEC made unallocated shelf registration available to foreign issuers in April 1994, although it has not extended this privilege to registrants filing pursuant to the U.S. MJDS. Unallocated shelf registration is already an important financing tool for domestic issuers and is likely to become one for foreign issuers as well since it increases the ability to take advantage of propitious market conditions on a regis-

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9. J. Quinn, *Summary of Activities Involving the Division of Corporation Finance, in* 2 SEC SPEAKS IN 1994 815 (1994). The SEC adopted the U.S. MJDS on June 21, 1991.

10. *Id.* at 797.

11. SEC 1993 ANNUAL REPORT, *supra* note 7, at 51.

12. Quinn, *supra* note 9, at 801. Unallocated shelf registration became available to domestic issuers effective October 29, 1992. Unallocated shelf registration allows a registrant to register debt, equity and other securities on one registration statement without indicating at the time of filing or effectiveness the amount of each type to be offered.

13. Kershaw, *supra* note 8. Again, Kershaw's figures include only transactions conducted by or through a placement agent and are under-inclusive to this extent.

14. Organization for Economic Cooperation and Development, *International Financial Markets*, 57 FIN. MARKET TRENDS, 54 62 (Feb. 1994) [hereinafter OECD 57 FIN. MARKET TRENDS].

15. *Id.* at 72-73.

16. *Id.* at 75.

17. DIVISION OF MARKET REGULATION, SECURITIES AND EXCHANGE COMMISSION, MARKET 2000: AN EXAMINATION OF CURRENT EQUITY MARKET DEVELOPMENTS II-13, II-14 (1994). "The trading of U.S. equities by U.S. broker-dealers on foreign exchanges amounts to several million shares per day. Most of this trading is done abroad because of time zone differences between the major markets in New York, Tokyo, and London." *Id.*

tered basis. The increase in cross-border securities transactions is associated with advances in automation, improvements in clearance and settlement systems, enhanced transparency of markets, new financial instruments and markets,[18] as well as issuers' voracious appetite for capital at the lowest possible cost. The internationalization of capital markets is as much a part of the liberal ideal as free trade since without free flow of and access to capital the benefits to be derived from an efficient allocation of world resources and division of labor are not fully attainable.[19]

The internationalization of securities regulation is a direct response to the increasing inter-dependence of the world's securities markets. Ironically, de-regulation is emerging as the approach of choice among national securities regulators, although it is a de-regulation focused not on domestic standards but rather on impediments to cross-border transactions that national regulators have been pursuing with studied persistence.[20] Thus, in 1993-1994 the SEC expanded access to short-form registration for foreign private issuers, extended unallocated shelf registration to them and made certain accommodations for their financial statements, expanded the class of Canadian issuers entitled to use MJDS, and granted exemptions from Rule 10b-6 for certain distributions by foreign issuers. In 1993-1994 Canada, for its part, expanded the availability of the Canadian Multijurisdictional Disclosure System ("CMJDS")[21] and adopted a ruling designed to facilitate private placements in Canada in connection with certain international offerings.[22] The European Union ("EU") adopted the Investment Services Directive in 1993 which will enable investment firms licensed in any EU member state to provide investment services throughout the Union on the basis of its home state license, and also adopted the controversial Capital Adequacy Directive which attempts to harmonize capital standards throughout the EU.[23] In May 1994, the European Union also adopted a measure that will allow companies with a specified reporting history in one member state to list throughout the Union without re-publication of full listing particulars.[24] Measures taken by national securities regulators to accommo-

18. *See* Organization for Economic Cooperation and Development, *Organization and Regulation of Securities Markets*, 54 FIN. MARKET TRENDS 14, 17-24 (Feb. 1993) [hereinafter OECD 54 FIN. MARKET TRENDS].

19. INTERNATIONAL CAPITAL MARKETS AND SECURITIES REGULATION § 1.01 (Harold S. Bloomenthal & Samuel Wolff eds., 1st & rev. ed. 1994) [hereinafter ICMSR].

20. *See* OECD 54 FIN. MARKET TRENDS, *supra* note 18, at 14-17 (deregulation of access to the securities industry, deregulation of commission rates, removal of restrictions on financial transactions, particularly foreign exchange transactions, and opening up domestic capital markets).

21. *See infra* § III[B].

22. *See infra* § II[B].

23. *See infra* § VI.

24. *See infra* § III[C].

date or facilitate international securities transactions have not been matched by any appreciable degree of regulatory progress on the international level.[25]

II. EXEMPT OFFSHORE OFFERINGS

A. *United States (Herein of Regulation S)*

It is impossible to gauge the full extent of unregistered offshore offerings by U.S. issuers made pursuant to Regulation S. In 1993, U.S. issuers borrowed $24.8 billion on international and foreign bond markets,[26] and presumably a large amount of these bonds were unregistered. In the same year, U.S. companies issued $9.9 billion of international equities.[27] OECD categorizes this amount as follows: "Euro-equities," $8.5 billion; "other international share placements," $1.4 billion.[28] A large portion of the $8.5 billion was probably sold pursuant to registration. One source estimates that since the "SEC approved Regulation S in 1990, $6 billion has been raised by U.S. companies via [Regulation S] issues."[29] The *Wall Street Journal* observed that, "[w]hile it is believed that billions of dollars have been raised through Regulation S transactions during the past four years, no one tracks these unregistered deals."[30]

1. Resales in the United States

Any resale into the United States of securities initially sold offshore under Regulation S will involve the means of interstate commerce and must be exempt from registration (or the securities must be registered). The exemptions that will usually be at issue in the case of resales outside of Rule 904 are Sections 4(1) and 4(3)[31] of the Securi-

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25. *See infra* § VII.

26. OECD 57 FIN. MARKET TRENDS, *supra* note 14, at 62.

27. *Id.* at 75.

28. OECD defines "Euro-equities" as "[n]ew issues and initial public offerings (IPOs) of common and preferred shares, participation certificates, 'certificates d'investissements' and similar instruments and international offerings taking place in the context of privatization." *Id.* at 76. n. 1 It defines "other international share placements" to include "secondary offerings, private placements, issues of redeemable convertible preference shares and internationally placed units of closed-end funds." *Id.* n. 2

29. *SAGA Offers Regulation S Fund to Non-US Funds*, INSTITUTIONAL INVESTOR, GLOBAL MONEY MANAGEMENT, Jan. 24, 1994, at 8. "Past issuers of 'S' stock include United Airlines in New York which raised $600 million, Newmont Mining ($295 million), Dell Computer Corporation ($23 million), and banking concern MidAtlantic, of Edison, New Jersey ($98 million)." *Id.* The Commission announced the adoption of Regulation S in Sec. Act. Rel. No. 6863, [1990 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,524 (Oct. 5, 1990) [hereinafter Release 6863].

30. Laurie R. Cohen, *Rule Permitting Offshore Stock Sales Yields Deals that Spark SEC Concerns*, WALL ST. J., April 26, 1994, at C1, col. 3.

31. Securities Exchange Act of 1934, § 4(1), 15 U.S.C. § 77(d)(1) (1988) (exempt-

ties Act and the safe harbor under these exemptions provided for by Rule 144A.[32] After the expiration of the restricted period, securities sold offshore may be resold in the United States to the extent that either Section 4(1) or Section 4(3) is available.[33] While Regulation S itself is silent on this point, the Release adopting Regulation S provides in a footnote stating that "[u]pon expiration of any restricted period, securities (other than unsold allotments) will be viewed as unrestricted."[34]

The staff has not issued any no-action letters, subsequent to the adoption of Regulation S which clarify the extent to which securities sold offshore may be resold in the United States. Moreover, in post-adoption informal discussions the staff is known to have pointed to Preliminary Note 6 for the proposition that securities acquired offshore may be resold in the United States only if registered or an exemption from registration is available. This assertion, of course, simply begs the question concerning the circumstances under which Section 4(1) is available for resales into the United States after the expiration of the restricted periods. The Commission, in the Releases proposing and adopting Regulation S, gave every indication that securities sold offshore pursuant to Regulation S would be unrestricted after the expiration of such periods.[35] If the offshore purchaser is relegated to Rule 144 for domestic resales the question naturally arises as to why the Commission expended so much effort to reduce the restricted periods previously established under Release 4708.[36] The result of such a construction would be that the abbreviated restricted periods of Regulation S would be of little practical benefit to offshore purchasers and, as the position became widely known throughout the industry, to issuers, distributors and other persons selling offshore.[37]

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ing "transactions by any person other than the issuer, underwriter or dealer"); *id.* at § 77(d)(3) (exempting certain transactions by dealers).

32. Private Resale of Securities to Institutions, 17 C.F.R. § 230.144A(d) (1994).

33. 15 U.S.C. § 77(d)(i) (1988).

34. Release 6863, *supra* note 29, at 80,676 n.110. The Release does not limit this statement to securities of reporting companies, although the statement appears in the section of the Release discussing so-called Category 2 securities (which include securities of reporting companies). *Id.*

35. *E.g.*, *id.* In the Release proposing Regulation S, the Commission discussed the resale offshore of securities privately placed in the United States. Note that the "restricted period" for Category 2 transactions in the initial Proposal was 90 days, and that Proposed Rule 906, the predecessor to the current resale rule, Rule 904, allowed a resale offshore pursuant to the same restrictions that applied to the issuer (with several exceptions).

36. The restricted period for offshore equity sales under Release 4708 was generally considered to be one year. The Commission proposed to reduce the restriction in Category 2 transactions to 90 days. Offshore Offers and Sales, 53 Fed. Reg. 22, 676 (1988) (proposed June 17, 1988). Upon reproposing the rules, the Commission proposed to reduce the proposed 90-day restricted period to 40 days. Revised Proposed Regulations, 54 Fed. Reg. 30,073 (1989) (proposed Sept. 13, 1989). This is the period actually adopted.

37. The ability to re-sell under Rule 904 on a DOSM is useful to purchasers, yet

On the other hand, confirmation by the staff that after expiration of the restricted periods offshore purchasers could re-sell in the United States privately or in routine trading transactions would codify an apparent contradiction between Regulation S and Rule 144. If, for example, common stock of a domestic reporting issuer is placed privately under Section 4(2) or Regulation D in the United States the securities are "restricted securities," the resale safe harbor for which under Rule 144 is two or three years, depending upon the circumstances.[38] If the same securities are sold offshore by the issuer under Rule 903 the restricted period, at least literally, is forty days.[39] The staff's post-adoption retreat into Preliminary Note 6 seems to be based upon the not unreasonable apprehension that this anomaly poses the potential for an abusive circumvention of Rule 144. Nonetheless, if the Commission insists on compliance with Rule 144 for resales in the United States of securities sold offshore, one of the principal purposes of Regulation S as reflected in its administrative history would seem to be severely compromised. It is unclear if, when or how this issue will be resolved.

In the meantime, confusion abounds in the industry and securities bar concerning the law of U.S. resales. At a March 1994 trade conference, the staff "shook up lawyers in the audience at a panel that discussed potential abuses of Regulation S . . . ."[40] A staff member explained that "she has seen a number of U.S. companies make substantial placements offshore at big discounts, only to sell them back into the United States."[41] The Director of Corporation Finance said that "'[i]f people are playing games, we are going to find them and we are going to take action,' . . . predicting that Regulation S cases will become a topic at next year's meeting."[42] At a different conference in March, the Director of Corporation Finance stated that "flowback" into the United States "in and of itself is not a problem." However, she told the group, if the Rule is being used to "'wait out the 40 days and get

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the staff had already partially accomplished this innovation through the no-action process under Release 4708. College Retirement Equities Fund, SEC No-Action Letter, [1987 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 78,420, at 77,362 (Feb. 18, 1987) (resales on Paris Bourse without investigation as to nationality of counterparty).

38. Rule 144 is not the exclusive means of re-selling restricted securities, however.

39. If securities are *resold* offshore pursuant to Rule 904, literally, the seller, except for dealers and persons receiving selling concessions, need not observe any restricted period. *See* Rule 904(c)(1). This construction assumes that Rule 904(c) supersedes statements to the contrary in the Release proposing Regulation S. Offshore Offers and Sales, Sec. Act Rel. No. 6779 [1987-1988 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,242 at 89,140 n. 131 (Sept. 26, 1988).

40. Karen Donovan, *SEC Officials Outline Agency's Agenda,* NAT'L L.J., MAR. 21, 1994, at B1, B3.

41. *Id.*

42. *Id.*

into the U.S. markets, that's a problem.'"[43] These developments were followed by a *Wall Street Journal* article, entitled "Rule Permitting Offshore Stock Sales Yields Deals That Spark SEC Concerns,"[44] reporting that a "little known but increasingly controversial Securities and Exchange Commission Rule known as Regulation S allows public companies to sell stock to offshore investors at substantial discounts without ever registering the shares with the SEC or telling stockholders about the sales."[45] The *Journal* quotes SEC Commissioner Roberts as saying "'[t]he indications of abuse of Regulation S may be sufficiently serious to call for a revisitation of the Rules by the Commission[.]'"[46] The Enforcement Division staff reportedly has indicated that the SEC is concerned about transactions by small, OTC companies that have privately placed large blocks of stock at discounts to market prices.[47] The staff has indicated that "in some cases, these Regulation S private placements appear to be 'schemes to evade registration requirements.'"[48] Finally, the *Journal* discussed a practice that has troubled the SEC: offshore investors selling short stock of a domestic issuer and replacing the borrowed shares with Regulation S stock.[49] The day following the *Journal* article, the Honorable Edward Markey (D-MA), chairman of the House Subcommittee on Telecommunication and Finance, wrote the SEC and requested a review of Regulation S and a report to Congress on whether the Rule should be repealed or modified.[50] Markey indicated that he was "'extremely concerned about indications of wide-spread abuses associated with Regulation S offerings.'"[51] Markey also asked for an analysis of the impact of the incentives the Rule creates for foreign speculators to drive down share prices and U.S. companies through short sales."[52] On May 6, 1994, Chairman Levitt responded in a two-paragraph letter to Markey as follows:

> This is in response to your letter dated April 27 expressing concern about possible abuses associated with Regulation S. The Commission has been aware for some time of situations in which unregistered offerings were purportedly made in reliance on Regulation S where such offerings may have been required to register under the Securities Act of 1933. In response, the Division of Enforcement and the Division of Corporation Finance are currently involved in a

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43. *Issuers "Pushing Envelope" of Reg. S Safe Harbor, Quinn Warns*, DAILY REP. FOR EXECUTIVES, Mar. 9, 1994, at 4, 6.

44. Cohen, *supra* note 30, at C1.

45. *Id.*

46. *Id.*

47. *Id.*

48. *Id.*

49. *Id.*

50. *See Markey Calls on SEC to Review Regulation S*, 20 CORP. FINANCING WEEK, May 2, 1994, at 14, 18.

51. *Id.*

52. *Id.*

> coordinated review of various offerings under Regulation S in an effort to determine the most effective method to address perceived and actual abuses in connection with unregistered offshore offerings.
>
> Over the last several months, the Commission's staff has discussed in public forums that it is reviewing offshore offering practices under Regulation S. As noted in these forums, this review may result in revisions to Regulation S as well as in one or more enforcement proceedings over the next several months. We will apprise you of any actions taken by the Commission to revise Regulation S.[53]

A wide range of choices confronts the practitioner trying to make his or her way through the morass of is Regulation S. At one extreme is the conservative practitioner who ceases to represent issuers and others engaged in Regulation S transactions until the SEC sees fit to clarify the law. At the other extreme is the more aggressive practitioner, who takes the position that not only does Regulation S speak for itself, it does so clearly, at least insofar as the offshore sale itself is concerned; and that Regulation S does not make distinctions based upon the price of securities (discount) at the health of companies. Such practitioners, zealously representing their clients within the bounds of the law, or at least the written law, or at least the written law as they see it, might advise their clients that it is permissible to engage in Regulation S transactions until the SEC repeals the rule, irrespective of the discount, the health of the company, etc. The unspoken assumption of this approach is that if the Administrative Procedures Act means anything, it means that speeches may not amend a rule of law. Although the appellate courts may ultimately sustain such a position, the aggressive practitioner may win the battle but lose the war after all of the litigation expenses are tallied.

A middle ground would be to advise clients not to engage in the type of transactions against which the staff railed in 1994, *viz.*, heavily discounted transactions, simultaneous short sales or use of derivatives, etc., especially where the principal market for the securities is in the United States. Similarly, a practitioner could advise the voluntary, contractual imposition of additional prophylactic measures, such as longer restricted periods, certifications of non-U.S. personhood during the restricted period, and certifications against short sales and use of derivatives. Another approach would be to assume that securities sold offshore pursuant to Regulation S in a transaction that would otherwise result in the securities being "restricted securities" within the meaning of Rule 144 may not be resold in the United States except in accordance with Rule 144 (or possibly Section 4(1 1/2)).[54] Until the

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53. Letter from SEC Chairman Levitt to Rep. Edward Markey (May 6, 1994).

54. Concerning Section 4(1 1/2), *see* Harold S. BLOOMENTHAL & HOLMES, ROBERTS & OWEN, SECURITIES LAW HANDBOOK § 10.02 (1994).

SEC amends Regulation S or makes its views known through an enforcement case, it is every practitioner for herself, but caution would appear to be the order of the day.

2. Legends

The offering restrictions, applicable to Category 2 and 3 safe harbors, require during the restricted period the use of a legend on the prospectus and in other offering materials and documents. Technically, the only legend required on a certificate is in connection with the sale of equity securities of a non-reporting U.S. company in reliance on the category 3 safe harbor.[55] The following legend literally complies with the requirements of Regulation S relating to certificates issued to purchasers of equity securities in reliance on the category 3 safe harbor:

> The securities covered by this Certificate have not been registered with the United States Securities and Exchange Commission under the Securities Act of 1933 ("the Act"). Holders of the securities prior to [day after expiration date of the restricted period] can resell the shares only if registered under the Act, pursuant to an exemption from registration under the Act, or in transactions effected in accordance with the provisions of Rule 904 of Regulation S adopted under the Act.[56]

The legend fails to reflect all of the nuances of Regulation S, and it may not be possible to do so in a meaningful fashion. Further, although the issuer-distributor safe harbor may not depend on it, the purchaser-investors are not fully informed by the foregoing legends of the conditions of their safe harbor or, insofar as the offering restrictions are concerned, that there are any restrictions on their resale. The following legend may be more informative in this respect:

> The securities covered by this Certificate have not been registered under the Securities Act of 1933 (the "Act") with the United States Securities and Exchange Commission and it is not intended that they will be registered. Prior to [day after expiration date of the restricted period] the securities cannot be offered or sold in the United States or to U.S. persons as defined by Rule 902(o) adopted under the Act, other than to distributors, unless the securities are registered under the Act, or an exemption from the registration requirements of the Act is available. Purchasers [Holders] of the securities prior to [day after expiration date of the restricted period] can resell the shares only pursuant to an exemption from registration under the Act, or in transactions effected outside of the United States [including transactions executed on the Exchange]

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55. SEC Regulations, 17 C.F.R. § 230.903(c)(3)(iii)(B)(3) (1994) (The issuer or seller could voluntarily place a legend on Category 1 or 2 securities as a prophylactic measure.).

56. *Id.*

> and provided they do not (and no one acting on their behalf) solicit purchasers in the United States or otherwise engage in selling efforts in the United States. A holder of the securities who is a distributor, dealer, subunderwriter or other securities professional, in addition, cannot prior to [day after expiration date of the restricted period] resell the securities to a U.S. person as defined by rule 902(o) of Regulation S unless the securities are registered under the Act or an exemption from registration under the Act is available.

One might add to all of the above legends a paraphrase of Preliminary Note 6 that might read as follows:

Thereafter [after the restricted period] the securities can be sold in the United States only if registered or if an exemption from registration is available.

If a legend is used with the "thereafter" clause attached, the combined statements add up to little more than a statement that the securities cannot be sold in the United States (or during the restricted period to a U.S. person) without registration or an exemption from registration. Such a message is singularly uninformative, and for this and possibly other reasons is unattractive to investors and transfer agents alike. Investors generally do not, of course, want a legend which interferes with the marketability of the securities. This is not to suggest that investors necessarily intend to transgress a restriction on resale when they buy restricted securities. Even if they fully intend to comply with the applicable restrictions investors still prefer to have unlegended securities because legends are simply one more impediment to selling. Except possibly when completely self-operating, (*e.g.*, until *X* date the securities may not be sold in the United States or to U.S. persons), legends usually require the investor, when he desires to resell, to obtain (and pay for) an opinion of counsel to persuade the transfer agent to transfer the securities. A legend of the type quoted above — "thereafter [after the restricted period] the securities can be sold in the United States only if registered or if an exemption from registration is available" — would surely prompt the transfer agent upon transfer instructions to request an opinion of counsel as to whether an exemption is available. Although the total absence of a legend presents the easiest case for a transfer agent, a self-operating legend (no resales in the U.S. or to U.S. persons until *X* date) would seem not require an opinion of counsel from the transfer agent's point of view. However, in today's litigious environment, many transfer agents would probably request an opinion anyway. A self-operating legend of the foregoing type does not, in fact, reflect the nuances of Regulation S.[57] Assume, for example, that on March 15, 1994 a

57. Legends, self-operating or otherwise, also are problematic if it is intended that the securities will trade on a stock exchange.

NASDAQ-traded issuer sells Category 2[58] securities to non-U.S. persons as part of an offshore distribution. A legend to the effect that until April 24, 1994 the securities cannot be resold in the United States or to U.S. persons is placed on the certificates (even though technically a legend is not required for Category 2 securities). The self-operating legend implies that on April 25, 1994 all of the securities may be re-sold in the United States, by any means, which may or may not be the case, depending upon how the SEC and courts apply Preliminary Note 6. Preliminary Note 6 states that offshore purchasers must find their own exemption for resales, and the staff is known to have stated informally that Preliminary Note 6 means exactly what it says. A legend reflecting only a forty-day restriction works uneasily in this context.

3. No-Action Letters

The staff has issued several no-action or interpretive letters under Regulation S since its promulgation, although most of them deal with issues that are somewhat tangential to the operation of Regulation S. Following is a discussion of several of these letters.

One of the "general conditions" of Regulation S is that no "directed selling efforts" be made in the United States by an issuer, a distributor, any of their respective affiliates, or any person acting for any of them.[59] "Directed selling efforts" are any activity undertaken for the purpose of, or that could reasonably be expected to have the effect of, "conditioning the market" in the United States for any of the securities being offered offshore.[60] Both the Regulation[61] and the Adopting Release[62] enumerate categories of activities that do not constitute directed selling efforts. Whether the dissemination in the United States of broker-dealer's quotations for securities offered offshore in reliance on Regulation S constitutes directed selling efforts is determined on "an individual interpretative basis."[63] Quotations in PORTAL are not deemed directed selling efforts.[64] Quotations of foreign broker-dealers distributed by a third party system primarily in foreign countries are not deemed directed selling efforts if (1) securities transactions cannot be executed with persons in the United States through the system, and (2) participants in the offering and foreign broker-dealers and other participants in the system do not initiate contacts with U.S. persons or persons within the United States beyond those contacts exempted

58. SEC Regulations, 17 C.F.R. § 230.903(c)(2) (1994). *See also supra* note 55 (technically, Category 2 securities need not be legended.)

59. SEC Regulations, 17 C.F.R. § 230.903(b) (1994).

60. SEC Regulations, 17 C.F.R. § 230.902(b)(1) (1994).

61. SEC Regulations, 17 C.F.R. § 230.902(b)(2)-(6) (1994).

62. Release 6863, *supra* note 29, at 80,669-71.

63. *Id.* at 80,671.

64. *Id.* at n. 71.

under Rule 15a-6.[65] In 1993 the staff indicated that a quotation on The Stock Exchange Automated Quotations ("SEAQ") system of a security of a foreign issuer does not constitute directed selling efforts provided that the quotation is not undertaken for the purpose of conditioning the market in the United States, and provided further that the issuer, distributors, their respective affiliates and persons acting on their behalf covenant not to, and do not, initiate contacts with U.S. persons or persons within the United States beyond those exempted by Rule 15a-6.[66] The staff gave a favorable response to this letter even though trading information concerning the securities quoted in SEAQ could be made available to U.S. persons and persons located within the United States. With respect to SEAQ quotations, the prohibition against contacts beyond those permitted by Rule 15a-6 only applies to the issuer, distributors, their affiliates and persons acting on their behalf and does not extend to other foreign broker-dealers and other participants in the system.[67]

In *Coral Gold Corporation*,[68] the staff took the position that the filing with the Commission under cover of Form 6-K of an offering circular pursuant to Rule 13a-16(b) would not constitute directed selling efforts where the circular contains no more information than is legally required by the laws of the foreign issuer's jurisdiction and bears a legend to the effect that the subject securities have not been registered under the Act and may not be offered or sold in the United States or to U.S. persons (other than distributors) absent registration or an exemption. The problem addressed in *Coral Gold Corp.* arises in other contexts in which disclosure requirements of U.S. or other law are at odds with prohibitions against directed selling efforts. For example, an offshore offering may be important to the registrant's liquidity and capital resources and thus otherwise merit discussion in the MD&A, yet it certainly would be possible to draw domestic attention, inappropriately, to an unregistered offshore offering through statements in the MD&A. Rule 135c, adopted in 1994, provides guidance in this regard.[69]

Resales of securities acquired in the United States or offshore may be made in "offshore transactions" pursuant to Rule 904 of Regulation S. One type of qualified "offshore transaction" for purposes of the resale safe harbor is a transaction executed in, on or through the facilities of a designated offshore securities market (DOSM) described in Rule 902(a).[70] Aside from the DOSMs specified in Rule 902(a)(1),[71]

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65. SEC Regulations, 17 C.F.R. § 230.902(b)(6) (1994).

66. Skadden, Arps, Slate, Meagher & Flom, SEC No-Action Letter, [1994 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 76,677 (May 18, 1993).

67. *Id.*

68. Coral Gold Corp., SEC No-Action Letter, [1992 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 79,707 (Feb. 19, 1991).

69. *See supra* § II[D].

70. SEC Regulations, 17 C.F.R. § 230.902(a) (1994) and SEC Regulations, 17

other foreign securities exchanges or "nonexchange markets" may qualify as DOSMs if "designated" by the Commission.[72] Subsequent to the adoption of Regulation S the SEC has designated the following markets as DOSMs: Helsinki, Mexican, Oslo, Alberta, Istanbul, and the Stock Exchange Automated Quotation (SEAQ) International.[73]

4. Public Announcements of Unregistered Offerings

An issuer that is making or has determined to make an unregistered private or offshore offering must balance the need to disclose or desirability of disclosing material information to the market with the countervailing obligation not to engage in a general solicitation,[74] or directed selling efforts in the United States,[75] as the case may be. Even though an issuer many not have a continuous, affirmative obligation to disclose to the market all corporate developments, even if material, it does have such an obligation under certain circumstances.[76] Aside from an obligation to disclose, an issuer may wish to disclose the fact that it is making or intends to make a private or offshore offering as this fact may be favorably perceived. Yet Regulations D and S clearly prohibit general solicitations, and directed selling efforts in the United States, respectively. To address these issues, in November 1993 the Commission proposed Rule 135c, a safe harbor for public announcements of unregistered offerings.[77] Rule 135c provides that for purposes of Section 5 of the Securities Act, an issuer's notice that it proposes to make, is making or has made an unregistered offering is not an "offer" (and therefore is not subject to the registration requirements) if it contains only limited, specified information concern-

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C.F.R. § 230.902(i)(1)(ii)(B)(2) (1994). ([N]either the seller nor any person acting on its behalf may know that the transaction has been pre-arranged with a buyer in the United States.)

71. SEC Regulations, 17 C.F.R. § 230.902(a)(1) (1994). The Eurobond market, as regulated by the Association of International Bond Dealers; Amsterdam Stock Exchange; Australian Stock Exchange; Bourse de Bruxelles; Frankfurt Stock Exchange; Stock Exchange of Hong Kong; International Stock Exchange of the United Kingdom and the Republic of Ireland; Johannesburg Stock Exchange; Bourse de Luxembourg; Borsa Valori di Milan; Montreal Stock Exchange; Bourse de Paris; Stockholm Stock Exchange; Tokyo Stock Exchange; Toronto Stock Exchange; Vancouver Stock Exchange; Zurich Stock Exchange.

72. SEC Regulations, 17 C.F.R. § 230.902(a)(2) (1994).

73. Shearson Lehman Hutton, Inc. (July 7, 1990) (Helsinki); Mexican Stock Exchange (Feb. 15, 1991); Oslo Stock Exchange (Dec. 13, 1991); Alberta Stock Exchange (Mar. 9, 1993); Istanbul Stock Exchange (Oct. 26, 1993); First Boston Corporation (June 14, 1990) *in* Stock Exchange Automated Quotation International (SEAQ).

74. SEC Regulations, 17 C.F.R. § 230.502(I) (1994).

75. SEC Regulations, 17 C.F.R. § 230.903(b) (1994).

76. *See generally* SFCL Chapter 9.

77. Simplification of Registration and Reporting Requirements for Foreign Companies; Safe Harbors for Public Announcements of Unregistered Offerings and Broker-Dealer Research Reports, Exchange Act Release No. 33,7029, [1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,252, at 84,689 (Nov. 3, 1993).

ing the issuer and the offering, and the conditions specified in Rule 135c are met.[78] The Commission adopted Rule 135c in April 1994[79] substantially as proposed except that the Commission limited reliance upon the Rule to reporting companies or companies complying with Rule 12g3-2(b). A notice of an unregistered offering will not qualify under the Rule if it is "used for the purpose of conditioning the market in the United States for any of the securities offered . . . ."[80] Rule 135c establishes other conditions and limits the information that may be included in the notice. Although the issuer may announce, *inter alia*, the "amount and basic terms of the securities offered,"[81] it is understood to be the staff's position that this phrase does not encompass the offering or selling price of the unregistered securities. This is consistent with the Release adopting Rule 135c which states that the information permitted by Rule 135c corresponds to that which is allowed under Rule 135.[82] Unlike Rule 134, which applies to communications after a registration statement has been filed, Rule 135 does not allow the disclosure of price. It is, however, permissible under Rule 135c (and Rule 135) to disclose the amount of the offering. Although Rule 135c applies most clearly in the context of a press release, the staff has indicated informally that the Rule provides appropriate guidance for discussions of unregistered offerings in publicly filed disclosure documents, including discussions and analyses of financial condition and results of operations. Management may wish to discuss unregistered financings in the liquidity and capital resources portion of the MD&A, but must be careful not to make a general solicitation or directed selling efforts in doing so.

B. *Canada*

In December 1993 the Ontario Securities Commission ("OSC") issued an order ("Blanket Ruling") designed to facilitate exempt transactions in Canada carried out in the context of an international securities offering.[83] The exemptions provided in Clauses (72)(1)(c)[84] or

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78. 15 U.S.C. § 135(c) (1988).

79. Simplification of Registration and Reporting Requirements for Foreign Companies; Safe Harbors for Public Announcements of Unregistered Offerings and Broker Dealer Research Reports, Exchange Act Rel. No. 33-7053, [1993-1994 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,331 (Apr. 19, 1994) [hereinafter Release 7053].

80. 15 U.S.C. § 135(c)(1) (1988).

81. 15 U.S.C. § 135(c)(3) (1988).

82. Release 7053, *supra* note 79, at 85,208. Rule 135 applies to notices to the effect that an issuer proposes to make a public offering.

83. Blanket Ruling In the Matter of the Securities Act, R.S.O. 1990, c. S.5, As Amended, and In the Matter of Regulation 1015, R.R.O. 1990, As Amended, and In the Matter of Certain International Offerings By Private Placement in Ontario, No. 5 Can. Sec. L. Rep. (CCH) ¶ 473-066 (Dec. 3, 1993) [hereinafter Blanket Ruling]. *See also Ontario Commission Removes Obstacles to Distributions by Certain Foreign Issuers*, INT'L SEC. REG. REP., Dec. 14, 1993, at 16, 18; Lococo, *OSC Rules on Private Placements*, 32 INT'L FIN. L. REV. 39, 39 (Jan. 1994); Edward Waitzer, *International*

72(1)(d)[85] of the Ontario Securities Act ("OSA"),[86] as modified by Subsection 27(1) of the Regulations ("Regulations") under such Act,[87] may be used by qualified U.S. and other non-Canadian issuers to sell securities in Ontario without compliance with the prospectus requirements of the OSA.[88] However, in general, an issuer delivering a disclosure document to a prospective investor in Ontario must give the investor a contractual right of action for rescission or damages against the issuer under certain circumstances and describe such right of action in the offering memorandum.[89] This allows an investor to rescind the transaction or obtain damages as a result of a misrepresentation in the disclosure document if the investor elects to pursue such remedy within 90 days from the initial payment for the securities.[90]

In December 1993, the Ontario Securities Commission ruled, pursuant to Subsection 74(1) of the OSA, that a distribution of securities in Ontario as part of an international offering of securities is not subject to the prospectus requirements of Section 53 of the OSA,[91] provided that (i) the issuer is a foreign issuer[92] (hereinafter "non-Canadian

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Securities Regulation-Coping With the 'Rashomon Effect', CANADA NEWSWIRE, April 11, 1994, 1, 4. Although this section is included in the subchapter entitled "Exempt Offshore Offerings by U.S. Issuers," it is recognized that a U.S. issuer may wish to sell in Canada securities that are registered under the U.S. Securities Act but exempt under provincial law in Canada.

84. This Section provides an exemption if the party purchasing is a person other than an individual and is recognized by the OSC as an exempt purchaser. Exempt purchaser status has been granted in the past to established institutional investors such as pension plans and mutual funds. *Ontario Securities Act*, R.S.O. 1990, § 72(1)(c).

85. Id. at § 72(1)(d), (together with applicable Regulations, provides an exemption if the investor purchases as principal and if the trade is in a security that has an aggregate acquisition cost to such purchaser of not less than $150,000).

86. *Id.* at c. S.5, as amended, 3 Can. Sec. L. Rpt. (CCH) ¶ 450-001.

87. *Regulations Under the Securities Act*, R.R.O. 1990, Can. Sec. L. Rep. (CCH) ¶ 452-001.

88. Other prospectus exemptions, without limitation, include: (1) rights offerings, as well as securities issued upon the exercise of rights; (2) sales of certain securities issued in connection with a statutory amalgamation or arrangement; (3) sales by an issuer of its own securities to employees; (4) certain "limited offerings"; and (5) placements of "Eligible Eurosecurities."

89. *See Regulations*, *supra* note 87, at § 32 (requiring provision of the contractual right of action under specified circumstances).

90. *Id.* (The investor is deemed to have relied upon the misrepresentation).

91. *Ontario Securities Act*, *supra* note 84, at § 53 (provides that no person shall trade in a security where such trade would be a "distribution," unless a prospectus has been filed and receipts therefor obtained from the director of the OSC).

92. Blanket Ruling, *supra* note 83. For purposes of the Blanket Ruling, a "foreign issuer" means an issuer that is not incorporated or organized under the laws of Canada or a province or territory of Canada, except where: (a) voting securities carrying more than 50 percent of the votes for the election of directors are held by persons whose address is in Canada; and (b) either: (i) the majority of the senior officials or directors of the issuer are citizens or residents of Canada; (ii) more than 50 percent of the assets of the issuer are located in Canada; or (iii) the business of

issuer"); (ii) the distribution of securities is made in accordance with an exemption provided by Clause 72(1)(c) or 72(1)(d) of the OSA, as modified by Subsection 27(1) of the Regulation (see above), *except* for the contractual right of action, which may be omitted; (iii) a non-Canadian disclosure document is delivered to an Ontario purchaser which includes either (A) a prospectus prepared in accordance with specified U.S. SEC registration forms[93] and pursuant to which an offering of securities concurrently is being made in the United States, (B) a private placement memorandum pursuant to which an offering of securities concurrently is being made in the United States,[94] or (C) a U.K. prospectus, which constitutes or includes "listing particulars" within the meaning of the Financial Services Act, is prepared in accordance with such Act and pursuant to which an offering of securities concurrently is being made in the United Kingdom.[95] In any case, the non-Canadian disclosure document must disclose that the securities being offered are those of a non-Canadian issuer and that the Ontario purchaser will not receive the contractual right of action otherwise required by Ontario law. Additional disclosure concerning remedies under U.S. or U.K. law must be provided. Specifically, the disclosure document must indicate that Ontario purchasers must rely on other remedies that may be available, including (in the case of a U.S. prospectus or private placement memorandum) "common law rights of action for damages or rescission or rights of action under the civil liability provisions of the U.S. federal securities laws."[96] The practical effect of the Blanket Ruling is to eliminate contractual rights of action in offerings that otherwise qualify for the specified exemptions.[97]

The Commission's ruling was based upon applications by market participants who represented to the OSC, *inter alia*, that "[i]n previous international offerings which have been extended into Ontario, some issuers and selling shareholders have expressed resistance, on both legal and logistical grounds, to the issuer providing a Contractual Right of Action and in the past, the [OSC] on application has granted full or partial relief from the requirement to give a Contractual Right

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the issuer is administered principally in Canada.

93. Securities Act of 1933, at S-1, S-2, S-3, F-1, F-2, or F-3.

94. If a U.S. private placement memorandum is delivered, the securities offered must be either those of a U.S. issuer, or those of a non-U.S. issuer, and the substantive preparation of the private placement memorandum must have involved of U.S. interstate commerce or other significant conduct in the United States.

95. *See* Blanket Ruling, *supra* note 83. *See also Ontario Commission Removes Obstacles to Distributions by Certain Foreign Issuers*, INT'L SEC. REG. REP., Dec. 14, 1993, at 2, 4.

96. Blanket Ruling, *supra* note 83, at 58,766. Lococo, *supra* note 83, at 39 ("It will be interesting to see whether some issuers, when faced with a requirement in the Blanket Ruling to alert investors to potential rights of action under U.S. or U.K. law, may not in some cases prefer to give the Ontario contractual right with its limited 90 days exercise period.")

97. *Id.* Lococo.

of Action on a case by case basis."[98] The applicants further represented that Ontario purchasers would have the benefit of various remedies under the Securities Act of 1933 or the Financial Services Act, as the case may be.[99] Although the contractual remedy would no longer apply if the terms of the Blanket Ruling are met, Ontario common law liability standards would remain applicable.[100]

As summarized by the OSC, the Ruling allows certain international offerings by non-Canadian issuers "to be made in Ontario by way of the exemptions contained in Clauses 72(1)(c) or 72(1)(d) . . . without requiring that purchasers in Ontario be given a contractual right of action against the issuer in compliance with Section 32 of the Regulation, provided that the offering concurrently is being made in the United States or the United Kingdom, specified U.S. or U.K. disclosure documents are being delivered to Ontario purchasers and other conditions are satisfied."[101] After the Blanket Ruling was announced, Societe Nationale ELF Aquitaine reportedly relied on it to facilitate an Ontario offering as part of a global offering.[102]

Separately, the OSC issued a letter on December 3, 1993, giving issuers permission to include in disclosure documents used in connection with international offerings made pursuant to the Blanket Ruling, a representation that the securities will be listed or quoted on a stock exchange or automated quotation system that includes at least the London Stock Exchange, a registered stock exchange in the United States or NASDAQ NMS. In order to qualify for this privilege, the application to list or quote the securities must have been made and the applicable conditions to the application must have been disclosed or satisfied.[103]

C. *Europe*

States that are members of the European Union (EU) must require that any offer of securities to the public "within their territories" be subject to the publication of a prospectus by the offeror, absent an exemption.[104] The directive is expressly inapplicable to certain types

98. Blanket Ruling for Certain International Offerings by Private Placement in Ontario, *supra* note 83. "In many offerings, the issuer has been unwilling to give such a right of action, especially where the proceeds of the offering accrue to a selling security holder rather than to the issuer. In addition, granting a contractual right of rescission raises corporate capacity problems in certain jurisdictions, including the United Kingdom, Ireland and Italy." Lococo, *supra* note 83, at 39.

99. The Securities Act of 1933, at §§ 11 or 12(2) or § 10(b) (depending upon the circumstances); or The Financial Services Act of 1986, at § 150.

100. Waitzer, *supra* note 83.

101. Blanket Ruling, *supra* note 83.

102. *See* Waitzer, *supra* note 83.

103. Blanket Ruling for Certain International Offerings by Private Placement in Ontario, *supra* note 83, at § 3a(3).

104. Council Directive of 17 Apr. 1989 Coordinating the Requirements for the

of offers and securities including "Eurosecurities which are not the subject of a generalized campaign of advertising or canvassing."[105] Member states are not required to enact this or other exemptions into national law and may make exemptions subject to limitations.[106] Most of the national laws of Western Europe recognize some type of private placement, professionals, or "Euro-"exemption, although practitioners must confirm the availability of such an exemption in any given case. In the U.K., the Companies Act provides that an offer of securities to persons "whose ordinary business it is to buy or sell shares or debentures (whether as principal or agent)" is not a public offer.[107] Thus, an issuer might offer securities to a professional investor, such as a fund manager, without a prospectus required by the Companies Act.[108] A U.K. commentator observes:

> [T]here has been much debate as to how wide the exemption goes. Many would argue that it does not extend to institutions such as insurance companies, however big their portfolios, because their 'ordinary business' is (for example) to provide insurance, not to deal in securities. Certainly, the exemption does not help if targeted investors in the UK are industrial corporates, again however large, unless their investments are managed by a dedicated treasury subsidiary[109] placement to purchasers who take the securities with investment intent.[110]

French law likewise recognizes exempt non-public offerings,[111] although the law in this area is somewhat vague and unsettled. In general, the securities may not be listed on an exchange, and further, may not be distributed beyond a circle of 300 persons, placed through financial institutions, advertised in the French media, or placed by way of customer solicitation to the residence or workplace of potential investors or in a public place.[112] Offers should be limited exclusively

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Drawing-Up, Scrutiny and Distribution of the Prospectus to be Published When Transferable Securities are Offered to the Public, art. 4. The directive applies to securities offered to the public for the first time in a member state if such securities are not already listed on a stock exchange in that state. *Id.*, art. 1.

105. *Id.*, art. 2, no. 2. "Eurosecurities" are transferable securities which are to be underwritten and distributed by a syndicate at least two of the members of which have their registered offices in different states; are offered on a significant scale in one or more states other than that of the issuer's registered office; and may be subscribed for or initially acquired only through a bank or other financial institution. *Id.*, art. 3.

106. Meredith Brown, *Global Offerings of Securities*, INT'L SECURITIES MARKETS, Aug. 12, 1992, at 287, 287-288.

107. Companies Act, 1985 § 79(2).

108. *E.g.*, Frank, Savory and Crosthwait, *United Kingdom*, in *Issuing Securities*, INT'L FIN. L. REV. 47 (Special Supp. Mar. 1993).

109. *Id.*

110. *Id.*

111. Thibaud, *France*, in *Issuing Securities*, *supra* note 108, at 22.

112. *Id.*

to professional and institutional investors, the offering document should state that the information contained therein may not be publicized and that resale of the securities in France is prohibited, and no subscription form should be attached to the document.[113] There must be no publicity to promote the offering and no canvassing of potential clients.[114] Other types of exempt offerings are (i) Euro-offerings qualifying as such under the EU's Prospectus Directive; (ii) certain mutual fund offerings; and (iii) certain offerings in connection with business combinations and related transactions.[115] "Issuers from non-OECD countries must in any event secure the approval of the Ministry of Finance for any offer of securities. There is no exemption for sales to sophisticated/professional investors as such."[116]

In Germany, the Stock Prospectus Requirements Act has been adopted to implement the EU's Prospectus Directive.[117] The Act contains a number of exemptions that are co-extensive with those permitted under the EU Prospectus Directive. Exemptions from prospectus requirements include, *inter alia*, securities offered solely to persons who purchase and sell securities for professional and trade purposes; securities offered solely to a restricted circle of persons; securities that may only be acquired in certain large denominations or amounts; and securities that qualify as "Euro-securities."[118] Although the availability of an exemption should be verified in any given case, as indicated, most or all of the other West European countries have exemptions for private placements, sales to securities professionals or Euro-offerings.[119] Thus it is quite possible for a U.S. issuer to offer a foreign tranche pursuant to Regulation S (or SEC registration) and exemptions from full foreign prospectus/listing requirements in most Western European countries. The parameters of prospectus exemptions in Europe must be confirmed on a case-by-case basis.

III. REGISTERED OFFSHORE OFFERINGS

A. *U.S. Registration*

It is becoming increasingly common for domestic issuers to include an offshore tranche when making a public offering in the United States. Section 5 applies extraterritorially in this context, unless the issuer complies with Regulation S and, absent such compliance, registration would be necessary unless another exemption were available. A

113. Brown, *supra* note 106, at 288.
114. *Id.*
115. Thibaud, *supra* note 111, at 22.
116. Brown, *supra* note 106, at 289.
117. ICMSR, *supra* note 19, at § 8C.07[4].
118. Brown, *supra* note 106, at 292.
119. Manning Warren, *Regulatory Harmony in the European Communities: The Common Market Prospectus*, 16 BROOK. J. INT'L L. 19, 46 n. 167 (1990).

domestic issuer making a U.S. public offering on a registered basis would have the option of either registering securities for the offshore offering as well, or complying with Regulation S for the international offering, since Regulation S generally would not require integration of a registered domestic offering with an unregistered offering under Regulation S, even if contemporaneous.[120] Including the international securities in the registration statement would necessitate paying a registration fee for the foreign tranche and ordinarily would involve two prospectuses, one foreign and one domestic. The staff's practice has been to allow both prospectuses to be filed as part of the same registration statement — typically, the complete prospectus for the U.S. offering would be filed, and alternate pages for the international prospectus would be included after the U.S. prospectus in the registration statement (before Part II of the registration statement). The alternate prospectus cover page reflects the international underwriters if a separate syndicate is being used to sell the securities offshore. A separate "Underwriting" section would describe the underwriting arrangements applicable to the offshore tranche. Typically, the registrant would enter into a separate underwriting agreement with the international underwriting syndicate.[121] Ordinarily, this agreement would provide, among other things, that the closing of the domestic offering would occur concurrently with the closing of the international offering. The international underwriters enter into an agreement among themselves and with the U.S. syndicate (inter-syndicate agreement), while the members of the international selling group also enter into an agreement.[122]

Registering the foreign tranche has the advantage of protecting the issuer from Section 5 concerns if the securities sold offshore flowed back to the United States. Particularly in light of the significant uncertainty concerning the resale in the U.S. of securities sold offshore,[123] registration of the foreign tranche is the method of choice when the issuer is undertaking registration anyway. Although under the alternative approach, *viz.*, selling the foreign tranche under Regulation S, the registrant would avoid Section 11 liability with respect to the offshore distribution, the risks to the issuer posed by untoward flowback, not to mention the discount associated with a lock-up, are probably not worth it.

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120. Release 6863, *supra* note 29, at 80,681.

121. *See, e.g.*, HAROLD S. BLOOMENTHAL, GOING PUBLIC HANDBOOK App. 47-1 (1994).

122. *Id.* at Apps. 47A, 47B, 47C.

123. *See* Resales in the U.S., *supra* § II(A)(1).

B. *Canadian MJDS*

The Canadian Securities Administrators amended the Canadian Multijurisdictional Disclosure System ("CMJDS") in December 1993 to make it more accessible to U.S. issuers.[124] In general, the amendments reduce the reporting history requirement for U.S. issuers, eliminate the $300 million market value requirement for offerings of certain securities, including common shares, eliminate the $150 million market value requirement for offerings of convertible investment grade debt, and accept determinations of investment grade status (*i.e.*, ratings) by SEC-recognized rating agencies. The discussion that follows summarizes the portions of the CMJDS that apply to offshore offerings by U.S. issuers of securities registered under the CMJDS, and reflects the December 1993 amendments.

The CMJDS[125] is available for several different types of offerings by U.S. issuers including offerings of investment grade securities, exchange bids, business combinations, rights offerings, and, if the issuer meets the "efficient market substantiality test,"[126] any other offering. Each of these categories requires, at a minimum, that the issuer meet a set of common eligibility requirements set forth in Section 3.2(1)-(5) of the Policy Statement. The issuer must be a "foreign issuer"[127] incorporated or organized under the laws of the United States or any state, territory, or the District of Columbia. Further, the issuer must be an SEC reporting issuer and have filed all required material[128] for

124. *E.g.*, *Securities Rule Changes*, THE FIN. POST, Dec. 16, 1993, at 13.

125. The Canadian Securities Administrators (CSA) adopted the CMJDS to serve as the counterpart to the multijurisdictional disclosure system concurrently adopted in the United States (MJDS or U.S. MJDS). Multijurisdictional Disclosure System, National Policy Statement No. 45 [hereinafter Policy Statement]. CMJDS was initially proposed by the Ontario Securities Commission (OSC) and the Commission des valeurs mobileres du Quebec (QSC), Canada's two leading securities commissions. Multijurisdictional Disclosure System, 12 O.S.C.B. 2919 (July 28, 1989), [Vol. 1] Can. Sec. L. Rep. (CCH) ¶ 10-192, at 3985; 20 Q.S.C. BULL. No. 29 (July 21, 1989). Subsequently, the Canadian Securities Administrators released Draft National Policy Statement No. 45. Draft National Policy Statement No. 45, [Vol. 1] Can. Sec. L. Rep. (CCH) ¶ 10-200, at 4186 (Nov. 1990) [hereinafter Draft Policy Statement]. CSA and the U.S. Securities and Exchange Commission (SEC) adopted the two measures in tandem.

126. Although not a defined term, the concept of a "substantiality" test, based upon the public float of the issuer's securities, plays a pivotal role in CMJDS. Any U.S. reporting issuer that has been such for 12 months and meets the substantiality requirement set forth in Section 3.3(2) (public float of U.S. $75 million) may use the CMJDS for the distribution of any security. Although only an approximation of market efficiency at best, for ease of reference this substantiality test is sometimes referred to herein the "efficient market substantiality test." There are lesser substantiality requirements associated with specific types of offerings under CMJDS as discussed below.

127. "Foreign issuer" is defined in Section 2(17) of the Policy Statement to exclude nominally foreign issuers that, in reality, are principally owned by Canadians or located in Canada. Draft Policy Statement, *supra* note 125, at § 2(17).

128. *Id.* at § 3.2(3). Specifically, the issuer must have filed all the material re-

the *12* calendar months preceding the filing of the preliminary prospectus with the principal jurisdiction,[129] special provision being made for successor issuers. Finally, the issuer must not be registered (or required to be registered) as an investment company under the U.S. Investment Company Act of 1940 and must not be a commodity pool issuer. In sum, to qualify for the system, the issuer must be a "foreign issuer" organized under U.S. law, or an SEC reporting company in compliance with its reporting obligations which is not registered or required to register under the Investment Company Act. These requirements, set forth in Section 3.2(1)-(5) of the Policy Statement, are hereafter referred to as the "Common Requirements." Another requirement, common to some but not all of the categories of transactions encompassed by CMJDS, is that the issuer "has had a class of its securities listed on the New York Stock Exchange or the American Stock Exchange or quoted on NASDAQ NMS for a period of at least 12 calendar months immediately preceding the filing of the preliminary prospectus with the principal jurisdiction and is currently in compliance with the obligations arising from such listing or quotation."[130] This requirement hereinafter is sometimes referred to as the "Listing Requirement."

The categories of offerings included within CMJDS are (i) nonconvertible investment grade debt and preferred shares; (ii) investment grade debt and preferred shares that may not be converted for at least one year after issuance, if the issuer meets a substantiality requirement; (iii) other securities, if the issuer satisfies the efficient market substantiality test; (iv) certain rights offerings, and business combinations and securities exchange bids. Compliance with the Common Requirements is necessary for each category. CMJDS is available for offerings certain derivative securities, namely, warrants, options, rights and convertible securities if the issuer of the underlying securities is eligible under the Policy Statement.

A seller may distribute investment grade debt and investment grade preferred shares in Canada, or rights immediately exercisable therefor, pursuant to CMJDS provided the issuer and the securities

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quired to be filed pursuant to Section 13, 14 or 15(d) of the Exchange Act for a period of at least 12 months immediately preceding the filing of the preliminary prospectus with the principal jurisdiction. *Id.* As originally, adopted, the reporting history requirement was 36 months. Although this condition requires the issuer to have filed all material required to be filed under the specified provisions prior to using MJDS, literally it does not require the information to have been timely filed. *Id.*

129. At the time of filing the preliminary prospectus in Canada the seller must select from among the provinces a "principal jurisdiction" to review the offering. The jurisdiction selected by the issuer to serve as principal jurisdiction may decline to serve as such.

130. *E.g.*, Draft Policy Statement, *supra* note 125, at § 3.4(2)(c). (special provision is made for successor issuers.).

satisfy the Common Requirements. This category includes securities having an "approved rating," as such term was amended in 1993.[131] Investment grade securities that are convertible are eligible for the system only if they are not convertible for at least one year and the issuer's equity shares have a public float of not less than U.S. $75 million.[132] Offerings of other securities, including, without limitation, common shares, also may be offered pursuant to the system, provided the issuer meets the Common Requirements and the issuer's equity shares have a public float[133] of not less than U.S. $75 million.[134] A U.S. issuer may use CMJDS for rights offerings if it meets the Common Requirements and the Listing Requirement,[135] except that for rights offerings a thirty-six month reporting history is required. The rights must be exercisable immediately upon issuance, and rights issued to a resident of Canada may not be transferable to another resident of Canada with certain exceptions.[136] Subject to the foregoing, rights issued to residents of Canada must have the same terms and conditions as rights issued to residents of the United States.[137] The Policy Statement provides an alternative eligibility requirement for certain guaranteed securities.[138]

A U.S. issuer contemplating an offering of securities in Canada should compare the process of financing pursuant to CMJDS to exempt

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131. "Approved rating," when used in relation to debt or preferred shares, means securities that have received a provisional rating by the Canadian Bond Rating Service Inc., Dominion Bond Rating Service Limited, Moody's Investors Service, Inc., or Standard and Poor's Corporation in one of the generic categories set forth in Section 2(4) of the Policy Statement. This definition is the same as that in CSA's shelf prospectus and delayed pricing system, a system that corresponds roughly to SEC Rules 415 and 430A. The Policy Statement was amended in December 1993 to accept ratings by any entity recognized by the SEC as a nationally recognized statistical rating organization, as that term is used in SEC Rule 15c3-1(c)(2)(iv)(F). (corresponding amendment to MJDS adopted by SEC in November 1993).

132. The further requirement that the issuer's equity shares have a market value of not less than $150 million was deleted in December 1993.

133. "Public float" means the aggregate market value of securities held by persons or companies not affiliates of the issuer. "Market value" (as used in the definition of "public float"), with respect to a class of securities, is the aggregate market value of the securities, calculated by using the price at which the securities were last sold in the principal market for the securities as of a date specified in the Policy Statement; or the average of the bid and asked prices of the securities in such market if there were no sales on the specified date.

134. The requirement that the issuer's equity securities have a market value of not less than U.S. $300 million was deleted in December 1993.

135. Draft Policy Statement, *supra* note 125, at § 3.4(2).

136. *Id.* at § 3.4(3)(c). (rights may be transferred to other Canadian residents who were granted rights of the same issue by the issuer.) In addition, the prohibition on transfer of rights does not affect transfer of securities issuable upon exercise of the rights, nor does it affect the transfer of rights on a securities exchange or interdealer quotation system outside of Canada. *Id.*

137. *Id.*

138. *Id.* at § 3.6

financing in Canada. Numerous possibilities of financing in Canada on an exempt basis are available.[139] Rather than qualifying securities for sale in Canada pursuant to CMJDS, a U.S. issuer might, for example, place an issue of securities on an exempt basis in Ontario with a consortium of banks, trust companies, insurance companies, government agencies, municipalities, or other recognized "exempt purchasers."[140] A U.S. issuer could also make an exempt placement in Ontario if the investor purchased as principal and made an investment of not less than $150,000.[141] The principal question for an issuer comparing CMJDS to exempt financing in Canada would be whether the discount in price associated with an exempt offering is sufficiently high to justify the time and expense associated with non-exempt financing. Exempt financing in Ontario in connection with international offerings of securities has been facilitated by a December 1993 Blanket Ruling by the Ontario Securities Commission.[142]

C. *Public Offers and Listing in the EU*

In May, 1994, the EU adopted new legislation designed to facilitate stock exchange listings in one member state by companies listed in other member states. The measure exempts companies that have been listed in other member states for at least three years from the requirement of publishing full listings particulars in the host state, although an abbreviated disclosure document must still be published. Provision is also made for companies the shares of which have been dealt in on second-tier markets. In general, the extent to which member states recognize both listing applications and prospectuses from companies outside the EU is left to the discretion of the member state. The following discussion of the listing and public offering process reflects the 1994 amendments to EU legislation.

The principal stock exchange directives concern the conditions to listing securities for trading on a stock exchange situated or operating within a member country[143] (the "Listing Conditions Directive") and the disclosure and filing requirements applicable to such listing (the "Listing Particulars Directive").[144] The Listing Conditions Directive sets forth minimum conditions for the admission of securities to listing on a stock exchange located in the EU.[145] These listing conditions involve matters such as the size of the issuer, its period of existence, and the distribution of its shares in the market.[146] The directive imposes

139. *Id.*
140. *See* Ontario Securities Act, *supra* note 84.
141. *Id.* at § 72(1)(d), Regs. 27(1).
142. *Id.*
143. Council Directive 79/279, 1979 O.J. (L66) 21.
144. Council Directive 80/390, 1980 O.J. (L100) 1.
145. Council Directive 79/279, *supra* note 143, at Preamble, art. 3.
146. *Id.* at Schedule A. For example, a company must, in general, have published

numerous responsibilities, including reporting obligations, on issuers of listed securities.[147] The directive does not prohibit the listing of shares from non-EC countries, but provides that if shares of such a company are not listed in the issuer's home country or principal market, they may not be listed in an EU country unless the authorities are satisfied that the absence of the home country/principal market listing "is not due to the need to protect investors."[148] Non-EU issuers listing in an EU country are required to meet the minimum conditions and obligations of the directive as enacted into national law in the particular country involved.

The purpose of the Listing Particulars Directive is to coordinate the differences in member state disclosure requirements applicable to stock exchange listing.[149] This directive requires member states to ensure that the listing of securities upon a stock exchange in their territory is contingent upon the publication of a disclosure document referred to as "listing particulars."[150] The Listing Particulars Directive allows a member state to create numerous exemptions. It also sets forth detailed disclosure requirements based upon whether the securities to be listed are debt or equity securities.[151] Listing particulars may not be published until they have been approved by the competent authorities,[152] but must be published for use by the investing public.[153]

The Listing Particulars Directive provides that when applications for listing the same securities on stock exchanges in several member states are made within short intervals of each other, the authorities in each state should cooperate with each other "to avoid a multiplicity of formalities and to agree to a single text," where appropriate.[154] The Listing Conditions Directive has a similar provision.[155] Subsequent to the adoption of the two principal directives, the Council adopted a directive requiring significantly further reciprocity in the listing process.[156] This directive applies when applications are made to list securities on two or more exchanges located in the EU, in which event listing particulars are to be prepared in accordance with home state rules and approved by home state authorities.[157] Once so approved,

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or filed its annual accounts for three financial years preceding the listing application. *Id.* at no. 3.

147. *Id.* at Schedule C and D.

148. *Id.* at Schedule A, no. 7.

149. Council Directive 80/390, *supra* note 144, at Preamble.

150. *Id.* at art 3.

151. *Id.* at art. 5 no. 1, Schedules A and B.

152. *Id.* at art. 18 no. 2.

153. *Id.* at arts. 3, 18, and 20.

154. *Id.* at art. 24.

155. Council Directive 79/279, *supra* note 143, at art. 18 no. 2.

156. Council Directive 87/345, 1987 O.J. (L185) 81.

157. *Id.*, amending the Council Directive 80/390 (Listing Particulars Directive),

"listing particulars must, subject to any translation, be recognized by the other Member States in which admission to official listing has been applied for, without it being necessary to obtain the approval of the competent authorities of those States and without their being able to require that additional information be included in the listing particulars."[158] If the issuer's registered office is not located in a member state, it must choose an EC country to supervise its listing.[159] The directive allows EC countries to restrict application of the foregoing mutual recognition rules to listing particulars of issuers having their registered office in a member state.[160] This is a common theme in the EU's regulatory scheme relating to the listing/public offering process. In 1993, the EU considered a proposal to exempt from the requirement to re-publish full listing particulars in a member state certain issuers with a three-year listing history in another member state.[161] As indicated above, the Council adopted the measure in May of 1994.[162] The 1994 amendment authorizes member states to allow the competent authorities to adopt an exemption from the requirement to publish full listing particulars where (i) the securities or the shares of the issuer have been officially listed in another member state for not less than three years before the application for listing; (ii) during such period (or such shorter period that the issuer's securities have been listed), "the issuer has complied with all the requirements concerning information and admission to listing imposed by Community Directives on companies the securities of which are officially listed;"[163] (iii) a simplified disclosure document meeting specified requirements is published.[164] The abbreviated disclosure document must contain, *inter alia*, a brief description of the securities; information specific to the market in which listing is sought (e.g., income taxes); the latest annual report,

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supra note 144, at art. 24.

158. Council Directive 87/345, *supra* note 156, at art. 24a. The authorities of any EC country may, however, compel the inclusion of certain limited information specific to the country in which listing is sought. *Id.*

159. *Id.*

160. *Id.* at art. 1, amending Council Directive 80/390, *supra* note 144, at art. 24.

161. *See Parliament Warns Listing Proposal May Discriminate Against Non-EU Firms*, INT'L SEC. REG. REP., Jan. 11, 1994, at 3, 5; *Stock Markets: Council Go-Ahead for "Eurolist" Directive,* EUROPEAN REPORT, Dec. 15, 1993, at 102, 102.

162. Council Directive 94/18, 1994 O.J. (L112) of the European Parliament and of the Council of May 30, 1994 Amending Directive 80/390/EEC 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, With Regard to the Obligations to Publish Listing Particulars. *See generally Council Gives Final Approval to Cross-Border Listing Measure*, 6 EUROWATCH 14, June 13, 1994; *EU Council Gives Final Approval to Key Cross-Border Listing Measure*, INT'L SEC. REG. REP, May 31, 1994, at 1; *EC Will Allow Additional Listings Without Publishing New Particulars*, SEC. REG. L. REP., May 20, 1994, at 737.

163. Council Directive 94/18, supra note 162, at art. 1. Note that the provision does not say, "substantially complied with" all of the applicable requirements.

164. *Id.*

audited annual accounts, and half-yearly report for the year in question if it has been published; any disclosure document published in the twelve months preceding the application; composition of management; capital; any auditors reports required by home country law.[165] This information must be sent to the competent authorities in the host state before being released to the public.[166] "[I]t is for that Member State to decide whether those documents should be scrutinized by its competent authorities and to determine, if necessary, the nature and the manner in which that scrutiny should be carried out[.]"[167]A parallel provision allows the listing on the basis of short-form particulars where a company's shares have been traded "for at least the preceding two years on a second-tier market" under specified circumstances.[168] In implementing the provisions of Directive 94/18, member states may establish "non-discriminatory minimum quantitative criteria."[169]

Directive 90/211 (the "Integration Directive") integrates disclosure in the listing and public offering process.[170] Directive 89/298 (the "Prospectus Directive") provides that where public offers are made within short intervals of one another in two or more member states, a public offer prospectus prepared and approved in accordance with the requirements for listing particulars must be recognized as a public offer prospectus in the other member states "on the basis of mutual recognition."[171] Under the Integration Directive, where application for listing in one or more member states is made and the securities in question were covered by a prospectus prepared and approved in any member state in accordance with the requirements for listing particulars in the three months prior to the listing application, the public offer prospectus must be recognized as listing particulars in the member state or states in which listing is sought.[172]

The Prospectus Directive coordinates the requirements for the drawing-up, scrutiny and distribution of a prospectus to be used when securities are offered to the public. Member states must require (absent an exemption) that any offer of securities to the public "within their territories" is subject to the publication of a prospectus by the offeror.[173] The directive is expressly inapplicable to certain types of

165. *Id.*
166. *Id.*
167. *Id.* at Preamble.
168. *Id.* at art. 1.
169. *Id.* at Preamble.
170. Council Directive 90/211, 1990 O.J. (L112) 24.
171. Council Directive 89/298, 1989 O.J. (L124) 8, 14.
172. Council Directive 87/345, *supra* note 156, at art. 2, amending Council Directive 80/390, *supra* note 144, at art. 24(b).
173. *Id.* at art. 4. The directive applies to securities offered to the public for the first time in a member state if such securities are not already listed on a stock exchange in that state. *Id.* at art. 1.

offers, including, without limitation, offers of securities to a "restricted circle of persons"[174] and "Eurosecurities which are not the subject of a generalized campaign of advertising or canvassing."[175]

The Prospectus Directive approaches public offerings on the basis of whether the securities in question will be listed in a member state. If a public offer of transferable securities is made in a member state and at the time of the offer the securities are the subject of a listing application in the same state, prospectus requirements must be determined in accordance with the Listing Particulars Directive as distinguished from Article 11 of the Prospectus Directive.[176] If a public offer is made in one member state and listing is sought on a stock exchange in another member state, the person making the public offering must have the possibility of using in the public offering a prospectus governed by the Listing Particulars Directive as opposed to the Prospectus Directive, in terms of both content and procedure, subject to any changes necessary to reflect the circumstances of the public offer.[177] Article 11 of the Prospectus Directive applies to public offerings of securities for which listing is not sought. Prospectuses for unlisted securities must be published or made publicly available pursuant to procedures established by each member state.[178] The member states *may* provide, however, that the person making the offering may prepare the prospectus, in terms of its content, and subject to appropriate adaptation, in accordance with the Listing Particulars Directive, even though the securities in question are not subject of a listing application.[179] In this event, prior scrutiny of the prospectus must be made by authorities designated by the member states.[180] A prospectus so prepared and approved by a member state in the three months preceding application for listing must be recognized, subject to translation, as listing particulars in the member states in which application for listing is made.[181] A prospectus so prepared in accordance with the Listing Particulars Directive must also be deemed to satisfy the prospectus requirements of other member states in which the same securities are, simultaneously or within a short time period, offered to the public.[182]

A member state may choose to allow issuers not proposing to apply for official listing to comply with Article 11 disclosure rather

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174. *Id.* at art. 2, no. 2.

175. Ontario Securities Act, *supra* note 84.

176. Council Directive 89/298, *supra* note 171, at art. 7.

177. *Id.* at art. 8(1). This possibility shall exist only in member states which in general provide for the prior scrutiny of public offer prospectuses. *Id.* at art. 8(2).

178. *Id.* at art. 15.

179. *Id.* at art. 12(1).

180. *Id.* at art. 12(2).

181. Council Directive 87/345, *supra* note 157, at art. 2, amending Council Directive 80/390, *supra* note 144, at art. 24(b)(1).

182. *Id.* at art. 21(1).

than compelling them to satisfy the same disclosure standards applicable to issuers concurrently applying for admission to official listing on an exchange in a member state. Further, a member state is not compelled to give such issuers the alternative of complying with the more stringent disclosure standards of the Listing Particulars Directive.[183] Under the Prospectus Directive, a member state has no obligation to recognize a prospectus meeting the requirements of another member state that satisfies only the Article 11 requirements.[184] Where public offers are made within short intervals of one another in two or more member states, a public offer prospectus prepared and approved in accordance with the Prospectus Directive, other than an Article 11 prospectus, must be recognized as a public offer prospectus in such member states.[185] The directive permits member states to limit this reciprocity requirement to issuers having their registered offices in a member state.[186]

IV. U.S. OFFERINGS BY FOREIGN ISSUERS

OECD reports that "[a] particularly noteworthy development [during 1993] was the growth of foreign bond issues in [the United States] where new offerings rose by 53 percent to $35.4 billion."[187] Canadian issuers accounted for almost one-third of the foreign bond issues in the U.S. during 1993.[188] OECD observes as follows:

> In addition to favourable interest rate conditions [during 1993], a particular attraction of the [U.S.] market continues to be the relative ease with which funds can be raised by lower-rated corporations and public sector bodies. The development of a broad and diversified market for private placements is also playing an important role in this respect, as indicated by the growing number of foreign borrowers accessing it either directly or through U.S.-based subsidiaries.[189]

IDD reports that foreign companies privately placed $50.1 billion of securities in the United States in 1993.[190] In 1993, foreign companies filed registration statements with the SEC covering over $46 billion of securities.[191]

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183. *Id.* at art. 12(1).
184. *Id.* at art. 21(1).
185. *Id.* at art. 21.
186. *Id.* at art. 21 no. 4.
187. OECD, 57 FIN. MARKET TRENDS, *supra* note 14, at 73.
188. *Id.*
189. *Id.*
190. Kershaw, *supra* note 8, at 18, 23.
191. SEC 1993 ANNUAL REPORT, *supra* note 7, at 51.

A. *Rule 144A Offerings*

Measurement of the 144A market may not be accomplished with precision because a Rule 144A offering is, in some respects, in the eye of the beholder. Conceptually, of course, Rule 144A deals primarily with the resale of securities and does not provide an exemption for an issuer engaged in a private placement. Nonetheless, it is designed to facilitate a specific type of private placement of an eligible security involving the purchase of an eligible security by a dealer in reliance on the Section 4(2) exemption and the resale of the securities to qualified institutional buyers in reliance upon Rule 144A. In reporting on the Rule 144A market to Chairman Dingell, the SEC stated that for purposes of such report, "a 'Rule 144A placement' is a transaction involving the sale of securities eligible for resale under Rule 144A which the market or market participants have identified as a Rule 144A placement."[192] Obviously, to be considered a 144A placement the securities must be eligible for resale under Rule 144A, and the information-supplying requirement, if applicable, must be satisfied.[193]

Other factors considered by market participants in determining whether an initial sale constitutes a Rule 144A placement include: whether private offerings are made to QIBs only; whether intermediaries purchase, as principals, from an issuer or distributor for immediate resales in reliance on Rule 144A; whether dealers buy in offshore transactions under Regulation S for immediate resale to QIBs in the United States under Rule 144A; whether the securities are eligible for trading through the Private Offering, Resale and Trading through Automated Linkages System (the "PORTAL system") operated by the National Association of Securities Dealers, Inc. (the "NASD"); and whether the securities are initially offered in placements in which the ability to negotiate the terms of the securities is more like that in a public offering than a traditional private placement.[194]

The statistics collected by the SEC and reported to Dingell relate to "144A placements" rather than all resales made in reliance upon Rule 144A. For example, an insurance company may resell securities it acquired a year ago in a private placement to another insurance company in reliance upon Rule 144A, but this does not necessarily involve a "Rule 144A placement."

Investment Dealers' Digest follows a similar approach in collecting its 144A statistics. IDD reports statistics based upon sales by or through investment and commercial banking firms serving as intermediaries in the 144A process.[195] (This would exclude privately negotiat-

192. U.S. SECURITIES AND EXCHANGE COMMISSION STAFF REPORT ON RULE 144A 1 (1993) [hereinafter SEC STAFF REPORT].

193. *Id.*

194. *Id.* at 2.

195. "Most 144A deals," an IDD report states, "are considered private placements

ed resales made in reliance on Rule 144A without the assistance of an intermediary). For the year ended December 31, 1993, IDD reports total "Rule 144A Private Placements" at approximately $91.3 billion, compared to $41.7 billion for the year ended December 31, 1992. Of the $91.3 billion of "Rule 144A Private Placements" during 1993, $66.8 billion was made by U.S. issuers and $24.5 was made by foreign issuers.[196]

In its report dated February 1993 to Chairman Dingell, the staff indicates that from April 1990, when 144A was adopted, to November 30, 1992, "$24.8 billion of securities relating to 206 issuers have been sold in 211 Rule 144A placements. Of this amount, $9.577 billion of securities relating to 128 foreign issuers . . . have been sold in 122 Rule 144A placements."[197] The $9.577 billion of securities issued (or guaranteed) by foreign issuers included roughly $4.8 billion of common stock, $4.5 billion of debt, and $338 million of preferred equity.[198] Thus, "Rule 144A placements have consistently been used in connection with the offer of foreign common equity securities on a private basis in the United States."[199]

B. *Registered Offerings*

The staff reports that foreign issuers are increasingly participating in the U.S. public markets:

> In 1993, more than $49.3 billion of foreign private issuer securities were filed for registration under the Securities Act. In 1993, 109 new foreign companies from 23 countries, including Argentina, Australia, Chile, China, Denmark, Germany, Italy, Korea, the United Kingdom and Venezuela entered the U.S. public markets. At the end of 1993, there were 588 foreign companies from 40 countries filing reports with the Commission.[200]

Thus, foreign issuers from all of the countries with developed capital markets have entered the U.S. public markets either by making a registered public offering in the United States or by registering a class of securities under the Exchange Act.[201] From January 1990 - February 1993, over 200 foreign issuers registered about $72 billion of

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by the Securities and Exchange Commission, but public securities by the market." Kershaw, *supra* note 8, at 16, 22-24.

196. *Id.* at 22-23.

197. SEC STAFF REPORT, *supra* note 192, at 3.

198. *Id.*

199. *Id.* (87 foreign issuers as of November 1992).

200. Quinn, *supra* note 9, at 797.

201. *See* Richard Kosnick, *Comments on Barriers to Foreign Issuer Entry into U.S. Markets*, L. & POL'Y INT'L BUS., June 22, 1993, at 1237, 1241. Examples of large foreign companies that have entered the U.S. public markets are Telefonos de Mexico, Societe Nationale Elf Aquitaine, Alcatel Alsthom, Grand Metropolitan PLC and Bass PLC. *Id.* at 1241-1242.

securities in over 300 registration statements.[202]

1. 1994 Amendments

The Commission proposed in 1993[203] and adopted in 1994[204] further rule changes relating to registration and reporting by foreign issuers, including registration on Form F-3. Currently, one of the "Transaction Requirements" for use of Form S-3 by a domestic company is that the aggregate market value of voting stock held by non-affiliates (public float) equal $75 million or more.[205] One of the "Registrant Requirements" for use of Form S-3 is that the registrant have been subject to the periodic reporting requirements of the Act for at least twelve months.[206] Prior to amendments adopted in 1994, the corresponding Form for foreign private issuers, Form F-3, provided for registrant eligibility, with certain exceptions, only if the public float of voting stock was $300 million or more and the issuer had been reporting for at least 36 months. Based upon "Commission experience with foreign issuers, as well as the internationalization of securities markets,"[207] in November 1993 the Commission proposed amendments to Form F-3 to lower the public float requirement of such Form from $300 to $75 million and to reduce the reporting history provision from 36 to 12 months.[208] The Commission reasoned that foreign issuers with a

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202. *Id.*

203. *See* Simplification of Registration and Reporting Requirements for Foreign Companies; Safe Harbors for Public Announcements of Unregistered Offerings and Broker-Dealer Research Reports, Sec. Act Rel. No. 33-7029, [1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,252 (Nov. 3, 1993) [hereinafter Release 7029]. In conjunction with its 1991 rights, tender and exchange offer proposals, the Commission proposed to amend Form F-3 to eliminate the three-year reporting and $300 million float requirements in connection with certain transactions. Cross-Border Rights Offers; Amendments to Form F-3, Sec. Act Rel. No. 33-6896, [1991 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,802 (Aug. 1, 1991). In Rel. 7029, the Commission stated that the 1991 proposals relating to secondary offerings, rights offerings, dividend or interest reinvestment plans, convertible securities and warrants "continue to be considered in light of public comment and issues raised by foreign disclosure practices." Release 7029, *supra* this note, at 84,686 n. 37.

204. Simplification of Registration and Reporting Requirements for Foreign Companies; Safe Harbors for Public Announcements of Unregistered Offerings and Broker-Dealer Research Reports, Sec. Act Rel. No. 33-7053, [1993-1994 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,331 (Apr. 19, 1994) [hereinafter Release 7053].

205. Form S-3, General Instruction I.B.1. The eligibility requirements for Form S-3 comprise "Registrant Requirements" and "Transaction Requirements." Any registrant that meets the Registrant Requirements may use the Form S-3 to register securities for a transaction that meets any of the Transaction Requirements. The public float requirement in Form S-3 was reduced to $75 million in Simplification of Registration Procedures for Primary Securities Offerings, Sec. Act Rel. No. 33-6964, [1992 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,053 (Oct. 29, 1992) [hereinafter Release 6964].

206. Form S-3, General Instruction I.A.3.

207. Release 7029, *supra* note 203, at 84,685.

208. *Id.* at 84,684.

public float of $75 million or more "have a degree of analyst following in their worldwide markets comparable to similarly-sized domestic companies."[209] The Commission adopted the November proposals in April 1994.[210] The revised Form F-3 eligibility provisions require the issuer to have filed at least one annual report prior to the first use of Form F-3. The April 1994 Release also amended Form F-3 to allow it to be used by otherwise eligible foreign issuers to register investment grade non-convertible preferred stock or any other investment grade non-convertible security irrespective of public float.[211] In addition, the Commission eliminated the public float requirement of Form F-3 with respect to qualified secondary offerings, rights offers, dividend or interest reinvestment plans, convertible securities and warrants.[212] The Form F-3 reporting requirement for issuers engaging in these transactions is twelve months.[213] Registration statements on Form F-3 relating to dividend or interest reinvestment plans will become effective immediately upon filing.[214]

Expanding F-3 eligibility to a wider class of foreign issuers concomitantly will make shelf registration available to more foreign issuers, as Rule 415(a)(1)(x)[215] under the Securities Act authorizes shelf registration of securities registered on Form F-3 to be offered and sold on a continuous or delayed basis by or on behalf of the registrant and certain others. The Commission also amended Item 512(a)(1) and 512(a)(4) of Regulation S-K to allow Form F-3 registrants to update shelf registration statements through incorporation by reference,[216] making a post-effective amendment unnecessary. In addition, the Commission has also extended "unallocated shelf registration" which is currently available to domestic issuers, to foreign issuers.[217] Unallocated shelf registration, as the name implies, allows a registrant to register debt, equity and other securities on one registration statement without indicating at the time of filing or effectiveness the amount of each type of security to be offered.[218] The staff reported that

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209. *Id.* at 84,685. *Cf.* Lee Spencer, *SEC Puts Out Welcome Mat for Foreigners*, N.Y.L.J., Dec. 6, 1993, at 9, 12 (positing potential argument of critics to the effect that "for U.S. investors, worldwide market following may not be as accessible, relevant or rigorous as analyst following in the U.S. market . . . [;] a foreign issuer may provide less disclosure in its 12 months as a reporting company than its domestic counterpart").

210. Release 7053, *supra* note 204.

211. Form F-3, *Id.* at 85,215, General Instruction I. B.2.

212. *Id.* at General Instruction I.B.3, I.B.4.

213. *Id.* at General Instruction I.A.1., I.A.2.

214. *Id.* at 85,217, General Instruction III.

215. *See* Rule 415 under the Exchange Act, 17 C.F.R. § 230.415.

216. Release 7053, *supra* note 204, at 85,204; *see also* Release 7029, *supra* note 204, at 84,685.

217. Release 7053, *supra* note 204, at 85,204; *see also* Release 7029, *supra* note 203, at 84,685.

218. *See* Release 6964, *supra* note 205, at 83,390 (the amount of the particular

through the end of 1993, 97 (domestic) issuers filed unallocated shelf registration statements covering $73.1 billion.[219] Unallocated shelf registration promises to be an important financing tool for foreign issuers as it will afford them increased flexibility to take advantage of propitious market conditions.

2. Financial Statements for Foreign Private Issuers

In November 1993 the Commission adopted a number of revisions to the rules governing financial statements of foreign private issuers.[220] The first set of revisions relates to aging requirements of financial statements included in the "F" Forms, which differ from those applicable to domestic issuers. In general, a foreign private issuer must include in the registration statement audited balance sheets as of the end of each of the most recent fiscal years, and audited statements of income and cash flows for each of the three fiscal years preceding the date of the two most recent balance sheet filed.[221] Prior to the amendments, Rule 3-19 required a registration statement under the Securities Act, on its effective date, to have financial statements as of an interim date within *six* months of such effective date; further, if the registration statement would become effective more than five months subsequent to fiscal year end, it was required to have audited statements for the most recent fiscal year.[222] Under the 1993 amendments, if the registration statement becomes effective within six months after fiscal year end, on its effective date the registration statement must include financial statements, which may be unaudited, as of a date within *ten* months of effectiveness.[223] If the audited statements for the most recent fiscal year are not available, they may be as of the two preceding fiscal years. If the filing becomes effective after six months subsequent to the end of the most recent fiscal year, it must include audited financial statements as of the end of the two most recent fiscal years.[224] Thus, a registration statement may become effective with audited statements 18 (rather than 17) months old,

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securities to be offered is established by prospectus supplement).

219. Quinn, *supra* note 9, at 801 (regarding conversion of an existing shelf registration statement to an unallocated registration statement); *see* 1992 WL 345024, Transitional Procedure for Converting to an Unallocated Shelf Registration Statement, SEC Interpretative Letter (Nov. 19, 1992).

220. Adoption of Final Amendments to Rule and Form Requirements Which Govern Age of Financial Statements of Foreign Private Issuers, Sec. Act Rel. No. 33-7026, [1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,247 (November 3, 1993) [hereinafter Release 7026].

221. *See* Regulation S-X, Rule 3-19(a), 17 C.F.R. 210.3-19(a).

222. Regulation S-X, Rule 3-19(b), 17 C.F.R. 210.3-19(b) (as revised as of April 1, 1988). Subject to these limitations, under the old rule, like the new one, if the issuer had recently passed the end of its fiscal year, the financial statements could be as of the end of the immediately preceding two years. *Id.*

223. Release 7026, *supra* note 220, at 84,6525. (Regulation S-X, Rule 3-19(b)).

224. *Id.* (Regulation S-X, Rule 3-19(c)).

and with unaudited interim statements ten (rather than six) months old.[225] The new framework is intended to provide foreign issuers (many of which are not subject to quarterly reporting requirements in their home country) "uninterrupted access to the public market."[226] Financial statements may be up to one year old at the effective date of the registration statement if the only securities are being offered pursuant to rights, transferable warrants, conversion rights, or dividend or interest reinvestment plans.[227] Notwithstanding the aging requirements, if the registrant discloses to its shareholders or otherwise makes public financial statements that are more current than is specifically required by Regulation S-X, those financial statements are to be included in the registration statement. However, under a 1993 amendment, interim financial information provided pursuant to Rule 3-19(f) need not be reconciled to U.S. GAAP if appropriate disclosure is provided.[228] In April 1994, the Commission proposed to allow domestic issuers making acquisitions of or investments in foreign businesses to follow the same aging rules with respect to the financial statements of the acquired foreign business and equity investees as those applicable to foreign private issuers registering or reporting under the securities laws.[229] The Commission adopted the amendments substantially as proposed.[230]

In April 1994[231] the Commission also took a noteworthy first step toward the internationalization of securities regulation by deciding to accept cash flow statements prepared in accordance with International Accounting Standard No. 7 without a reconciliation to U.S. GAAP.[232] The measure constitutes the first time the Commission has accepted an International Accounting Standard without requiring reconciliation to U.S. GAAP.[233] Former SEC Commissioner Karmel calls this development "a major conceptual breakthrough," adding that "[a]lthough the SEC's decision to recognize IAS no. 7 as authoritative is only a small step in this direction, and may prove to have little practical signifi-

225. *See* Spencer, *supra* note 209, at 9.

226. Release 7026, *supra* note 220, at 84,650.

227. Rule 3-19(e), 17 C.F.R. 210.3-19(e).

228. Release 7026, *supra* note 220, at 84,651.

229. Financial Statements of Significant Foreign Equity Investees and Acquired Foreign Businesses of Domestic Issuers and Financial Schedules, Sec. Act Rel. 7055, [1993-1994 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,333, at 85,232 (Apr. 19, 1994) [hereinafter Release 7055].

230. Financial Statements of Significant Foreign Equity Investees and Acquired Foreign Businesses of Domestic Issuers and Financial Schedules, Sec. Act Rel. No. 33-7118 [1994 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,665 (Dec. 30, 1994) [hereinafter Release 7118].

231. Release 7053, *supra* note 204, at 85,205 (adoption); Release 7029, *supra* note 203, at 85,252 (proposal).

232. *Id.* at 84,687.

233. Spencer, *supra* note 209 (discussing International Accounting Standards generally).

cance, it is the first time the SEC has been willing to concede that any accounting standard other than U.S. GAAP might be acceptable financial disclosure."[234] In tandem with its recognition of IAS no. 7, the SEC showed its support for another international standard, IAS No. 22, by proposing (in April 1994) "to eliminate the requirement that foreign private issuers quantify the effects of differences arising solely from the different criteria applied to the selection of the basic method of accounting for a business combination if the criteria used in the primary financial statements for determining the method are consistently applied and are consistent with IAS 22."[235] The amendments were adopted substantially as proposed.[236]In addition, in April 1994 the Commission proposed that "foreign private issuers that have consistently applied accounting policies which amortize goodwill and negative goodwill over periods which comply with the amended guidance in IAS 22, but which differ from the periods that would be permitted under U.S. GAAP, . . . not be required to quantify the effects of that difference in the reconciliation."[237] This amendment was adopted substantially as proposed.

Another amendment the Commission adopted in 1994 relates to transitional reconciliation requirements for foreign private issuers. Specifically, the Commission decided to reduce on a transitional basis the number of years for which foreign issuers filing a Form 20-F for the first time must reconcile their financial statements and selected financial data to U.S. GAAP.[238] Under the amendments, reconciliation is required for first time registrants only for the two most recently completed fiscal years; however, "[i]n each subsequent year, on a prospective basis, an additional year of reconciliation would be required up to the full reconciliation otherwise required."[239] "In response to comments, Form 20-F will be clarified to indicate that the transitional reconciliation relief also applies to financial disclosures required by U.S. GAAP and Regulation S-X."[240] The Commission also determined to allow reconciliation to U.S. GAAP pursuant to Item 17 (as opposed to the more stringent Item 18) of Form 20-F for any offering of invest-

234. Roberta Karmel, *New Initiatives for Foreign Issuers*, N.Y.L.J., Dec. 16, 1993, at 3, 7.

235. Reconciliation of the Accounting by Foreign Private Issuers for Business Combinations, Sec. Act Rel. No. 33-7056, [1993-1994 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,334, 85,241 (Apr. 19, 1994) [hereinafter Release 7056]. Differences in procedures used to implement either the purchase or pooling method would continue to be quantified. *Id. See also infra* note 249.

236. Reconciliation of the Accounting by Foreign Private Issuers for Business Combinations, Sec. Act Rel. No. 33-7119 [1994 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 86,756 (Dec. 13, 1994) [hereinafter Release 7119].

237. Release 7056, *supra* note 235, at 85,241.

238. Release 7053, *supra* note 204, at 85,206.

239. Release 7029, *supra* 203, at 84,687.

240. Release 7053, *supra* note 204, at 85,206.

ment grade securities.[241] The Commission has also (i) waived reconciliation of the separate financial statements of acquired businesses and less than majority owned "investees" under certain circumstances;[242] (ii) decided to accept compliance with Item 17 of Form 20-F for financial statements of all significant acquirees and investees;[243] (ii) made certain accommodations for foreign private issuers using pro rata consolidation (as opposed to the equity method) for joint ventures;[244] (iii) eliminated the requirement that foreign private issuers furnish certain financial statement schedules,[245] and proposed the elimination of these schedules for domestic issuers and other schedules[246] for both foreign and domestic issuers;[247] (iv) proposed to allow flexibility in the selection of the reporting currency used in SEC filings;[248](v) proposed to streamline financial statement reconciliation requirements for foreign private issuers with operations in countries with hyperinflationary economies;[249] and (vi) proposed to eliminate the requirement under present Rule 3-09 of Regulation S-X that total assets be considered in determining whether financial statements of a less

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241. *Id.*

242. *Id. See also* Release 7055, *supra* note 229, at 85,231 (proposing to extend same position to domestic issuers making foreign acquisitions or investments).

243. Release 7053, *supra* note 204, at n. 42 and accompanying text. "Frequently, the information required by Item 18 of Form 20-F regarding U.S. GAAP and Regulation S-X is more difficult to obtain for financial statements of acquirees and investees than for the issuer, but it is typically less critical to an understanding of the issuer's financial condition." *See also* Release 7055, *supra* note 229, at 85,231 (proposing to give domestic issuers the same privilege in reporting financial statements of significant foreign business acquisitions or foreign equity investees).

244. Release 7055, *supra* note 229, at 85,207.

245. *Id.* The following schedules have been eliminated for foreign private issuers: marketable securities; amounts receivable from related parties and underwriters, promoters and employees other than related parties; indebtedness of and to related parties — not current; property, plant and equipment; accumulated depreciation, depletion and amortization of property, plant and equipment; guarantees of securities of other issuers. *Id.* at 85,232.

246. *Id.* at 85,233 (proposing short-term borrowings; supplementary income statement information; other investments).

247. *Id.*

248. Selection of Reporting Currency for Financial Statements of Foreign Private Issuers and Reconciliation to U.S. GAAP for Foreign Private Issuers with Operations in a Hyperinflationary Economy, Sec. Act Rel. No. 33-7054, [1993-1994 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,332 (Apr. 19, 1994) [hereinafter Release 7054]. Current rules require presentation of financial statements in the currency of the country of incorporation or the primary economic environment. A revision to Rule 3-20 of Regulation S-X has been proposed to allow a foreign issuer to present its financial statements in any currency in which it reports to a majority of non-affiliated securityholders. *Id.*

249. *Id.* "[T]he Commission is proposing to eliminate the requirement of Items 17 and 18 of Form 20-F that an issuer quantify the effects on financial statements of its use of a translation methodology for operations in a hyperinflationary environment which differs from SFAS 52 so long as it conforms with IAS 21, provided that the method used is consistently applied in all periods." *Id.* at 85,227.

than majority owned equity investee (foreign or domestic) must be provided.[250] The foregoing amendments were adopted substantially as proposed.[251]

C. *U.S. MJDS*

Concerning use of MJDS to date by Canadian issuers, staff members report as follows: "Through December 24, 1993, there were 70 filings under the Securities Act by 50 Canadian issuers using the MJDS. A total of $11.54 billion of securities have been registered under the MJDS. Thirteen of these MJDS have involved non-underwritten rights offerings and eight have involved exchange offers."[252] These statistics do not include use of the Canadian MJDS by U.S. issuers,[253] statistical information as to which is scanty.

The U.S. MJDS gives qualifying Canadian registrants the opportunity to make securities offerings in the United States on the basis of, for the most part, Canadian disclosure requirements.[254] The Commission amended MJDS in June 1993[255] and again in November 1993.[256] Both the June and November amendments are based upon an April 1993 rule proposal by the Commission.[257] Specifically, the

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250. Release 7055, *supra* note 229, at 85,231.

251. Selection of Reporting Currency For Financial Statements of Foreign Private Issuers and Reconciliation to U.S. GAAP for Foreign Private Issuers with Operations in a Hyperinflationary Economy, Sec. Act Rel. No. 33-7117 [1994 Transfer Binder] Fed. Sec. L. Rep. (CCH) 77,001 (Dec. 30, 1994); Financial Statements of Significant Foreign Equity Investees and Acquired Foreign Businesses of Domestic Issuers and Financial Schedules, Sec. Act Rel. No. 33-7118 [1994 Transfer Binder] Fed. Sec. L. Rep. (CCH) 77,500 (Dec. 30, 1994).

252. Quinn, *supra* note 9, at 815.

253. *Id.*

254. The system also extends to qualifying tender offers and exchange offers. Finally, the system enables qualifying Canadian companies that otherwise would be subject to U.S. continuous disclosure, proxy, and insider reporting rules to observe, instead, corresponding Canadian requirements. The objective of the MJDS is "to facilitate cross-border offerings of securities and continuous reporting by specified Canadian issuers," and thereby to "remove unnecessary impediments to transnational capital formation." Multijurisdictional Disclosure and Modifications to the Current Registration and Reporting Systems for Canadian Issuers, Sec. Act Rel. No. 33-6902, [1991 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,812, 81,861 (June 21, 1991) [hereinafter Release 6902].

255. Amendments to the Multijurisdictional Disclosure System for Canadian Issuers, Sec. Act Rel. No. 7004 (June 28, 1993), [1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,207 [hereinafter Release 7004].

256. Amendments to the Multijurisdictional Disclosure System for Canadian Issuers, Sec. Act Rel. No. 33-7025, [1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,246 (Nov. 3, 1993) [hereinafter Release 7025].

257. Amendments to the Multijurisdictional Disclosure System for Canadian Issuers, Sec. Act Rel. No. 33-6997, [1992-1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,135, at 84,136 (Apr. 28, 1993) [hereinafter Release 6997]. The Commission also proposed a change to Form F-7 relating to agents for service of process, issued interpretive advice concerning the registration of warrants and convertible or exchange-

Commission proposed to modify the eligibility requirements for Forms F-9 and F-10 under the Securities Act, accept ratings by recognized *Canadian* (in addition to U.S.) rating organizations and rescind a sunset provision of then-current law that would have automatically eliminated financial statement reconciliation requirements of Forms F-10 and 40-F.[258] In June 1993 the Commission decided to retain the financial statement reconciliation requirement of Forms F-10 and 40-F.[259] In November 1993 the Commission adopted almost all of the other proposals.[260]

Form F-10, in general, is available for any type of security, including common equity and non-investment grade debt, and any type of offering, by a Canadian private issuer that satisfies specified eligibility requirements.[261] The financial statements included in Form F-10 must be reconciled to U.S. GAAP in accordance with Item 18 of Form 20-F.[262] As originally adopted, MJDS provided that such reconciliation would only be required for registration statements on Form F-10 filed prior to July 1993. Form 40-F permits eligible Canadian issuers to register or report under the Exchange Act essentially by filing with the SEC a wrap-around of materials they are required to file with Canadian regulatory authorities. As originally adopted, MJDS required Forms 40-F filed prior to July 1993 (with certain exceptions) to include a reconciliation to U.S. GAAP in accordance with Item 17 of Form 20-F.[263] Thus, absent Commission action, the reconciliation requirements for both Forms F-10 and 40-F would have lapsed in July 1993. The June 1993 amendments to Form F-10 and Form 40-F continued indefinitely the requirement that financial statements included in such Forms present a reconciliation to U.S. GAAP.[264]

Form F-9 is available for the registration of investment grade debt or preferred securities and extends to convertible investment grade securities only if they cannot be converted for a period of at least one year after issuance.[265] Prior to the November 1993 amendments,

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able securities on such Form and requested comments concerning unallocated shelf registration of aggregate amounts of securities. *Id.* at 84,139-40. In the November 1993 Release the Commission adopted the proposed amendment to Form F-7 relating to specifying an agent for service of process. Release 7025, *supra* note 256, at 84, 646.

258. *Id.* at 84,136.

259. Release 7004, *supra* note 255.

260. The unallocated shelf proposal was not adopted. However, Canadian issuers may use this procedure in connection with conventional registration to the same extent as other foreign issuers.

261. There are special provisions applicable to exchange offers, business combinations, and derivatives. See Release 6902, *supra* note 254, at 81,904.

262. Form F-10, Release 7004, *supra* note 255, at 84,237.

263. Form 40-F, *Id.* at 84,238.

264. *Id.* at 84,235.

265. Form F-9, Release 6997, *supra* note 257, at 84,136-37.

Form F-9 required the registrant to be a Canadian private issuer or crown corporation subject to the continuous disclosure requirements of any Canadian securities commission or equivalent regulatory authority for 36 consecutive months (12 months, in the case of a crown corporation) and currently in compliance with such reporting requirements. Further, prior to such amendments, in order to register convertible securities on Form F-9 the issuer also had to satisfy a "substantiality requirement" measured by market capitalization of (CN) $180 million and public float of (CN) $75 million.[266] As indicated above, Form F-10 is available for the registration under the Securities Act of any type of security (except certain derivatives) and offering by a Canadian private issuer, provided the issuer satisfies the eligibility requirements, including a substantiality requirement.[267] Prior to the November 1993 amendments, the market capitalization of the issuer's outstanding equity securities was required to be (CN) $360 million and its public float had to be at least (CN) $75 million in order to use Form F-10.[268] Further, the issuer was required to have been subject to the continuous disclosure requirements of any Canadian securities commission or equivalent regulatory authority in Canada for 36 consecutive months and currently be in compliance with such reporting requirements. In April 1993 the Commission proposed to modify the eligibility requirements for use of Forms F-9, F-10 and 40-F by completely eliminating the market capitalization threshold, setting the public float threshold at *U.S.* $75 million,[269] and reducing the reporting history requirement to 12 months. In November 1993 the Commission adopted these proposals.[270] Amendments to the Canadian MJDS followed in December 1993.[271]

V. TRADING PRACTICES RULES

A. *Background*

Rule 10b-6 of the Exchange Act makes it unlawful for certain persons interested in a distribution of securities, by the use of the means of interstate commerce, to bid for or purchase any security which is the subject of such distribution, or any security of the same class and series, or to attempt to induce any person to purchase any such security, until after he has completed his participation in the

266. *Id.* at 84,137.

267. Form F-10, Release 6902, *supra* note 254, at 81,904.

268. *Id.*

269. Release 6997, *supra* note 257, at 84,137. Insofar as Form F-9 is concerned, these changes only impact convertible securities, since the market capitalization and public float requirements do not apply if the securities being registered are not convertible. Form F-9, *Id.* at 84,142.

270. Release 7025, *supra* note 256, at 84,643-44.

271. *Id.*

distribution.[272] This prohibition applies to an underwriter, or prospective underwriter, of a particular distribution; the issuer, or other person on whose behalf the distribution is being made; any broker, dealer or other person who has agreed to participate or is participating in the distribution; and any "affiliated purchaser."[273] For purposes of Rule 10b-6 only, a "distribution" is an offering of securities, whether or not subject to registration under the Securities Act, that is distinguished from ordinary trading transactions by the magnitude of the offering and the presence of "special selling efforts and selling methods."[274] Rule 10b-6 contains a number of exceptions, including one for stabilizing transactions made in accordance with Rule 10b-7[275] and one adopted in 1993 for passive market-making.[276] Rule 10b-8 contains detailed provisions governing the distribution of securities through rights. Rule 10b-6, 10b-7 and 10b-8, are referred to herein, as the "Trading Practices Rules."

Rule 10b-6 does not, by its terms, limit itself to bids and purchases by U.S. persons, bids and purchases for securities issued by U.S. persons or bids and purchases made in the U.S. capital markets, and accordingly the Rule has been a major issue in many international and multinational securities offerings.[277] If the issuer or seller is making a distribution in the United States, the SEC traditionally has asserted that Rule 10b-6 applies on a worldwide basis to all distribution participants and their affiliated purchasers (absent an exception or exemption).[278] The Rule would thus generally apply in the case of offshore

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272. 17 C.F.R. § 240.10b-6 (1995)[hereinafter Rule 10b-6].

273. *Id.* at Rule 10b-6(a)(1)-(4). *See* Rule 10b-6(c)(6)(i) (defining "affiliated purchaser").

274. *Id.* at Rule 10b-6(C)(5).

275. *Id.* at Rule 10b-6(a)(4)(viii). The Commission also has the authority to exempt any transaction from Rule 10b-6 as not comprehended within the purpose of the Rule. *See* Rule 10b-6(h).

276. Passive Marketing Making, Sec. Act Rel. No. 33-6991, [1992-1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,126 (Apr. 8, 1993).

277. *See, e.g., International Equity Offerings and Market Making Activities on Foreign Stock Exchanges under Rule 10b-6: Has the Securities and Exchange Commission Gone Too Far?*, 14 BROOK. J. INT'L L. 389 (1988) [hereinafter *International Equity Offerings*].

278. Application of Rules 10b-6, 10b-7, and 10b-8 During Distributions of Securities of Certain Foreign Issuers, Sec. Act Rel. No. 33-7027, [1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,248, at 84,654 (Nov. 3, 1993) [hereinafter Release 7027]. Where foreign activities have or may have an impact on domestic securities markets, "the Commission has taken the position that Rule 10b-6 applies to all of the distribution participants and their affiliates," wherever located. Request for Comments on Issues Concerning the Internationalization of the World's Securities Markets, Exchange Act Rel. No. 34-21958, [1984-1985 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,759, at 87,392 (Apr. 18, 1985). The SEC's position concerning the extraterritorial application of Rule 10b-6 is based upon the premise that trading in foreign markets "could have the manipulative effect upon distributions in the United States that the Trading Practices Rules are designed to prevent." Release 7027,

distributions conducted pursuant to Regulation S if the issuer or seller also is making a distribution in the United States. Subject to the new exception discussed below, a Rule 144A offering could also constitute a "distribution" subject to Rule 10b-6, depending upon the magnitude of the offering and the presence of special selling efforts.[279] While the SEC has made a very broad assertion of extraterritorial jurisdiction in the area of Rule 10b-6, it has granted exemptive or no-action relief on both individual and class bases on numerous occasions.[280]

B. *144A Transactions*

In November 1993 the Commission amended the Trading Practices Rules to exempt from the prohibitions thereof distributions of certain foreign securities to qualified institutional buyers.[281] The securities must be eligible for resale under Rule 144A(d)(3)[282] and may be offered or sold in the United States only to qualified institutional buyers ("QIBs")[283] in transactions exempt under Section 4(2) of the Securities Act,[284] or Regulation D[285] or Rule 144A under such Act.[286] Although the requirement that sales be limited to QIBs only applies to the U.S. tranche,[287] the exception provided by Rule 10b-6(i) extends to transactions in all markets, both domestic and foreign.[288] Thus, a foreign issuer could sell the U.S. tranche to QIBs and qualify for ex-

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supra this note, at 84,654.

279. Exceptions to Rules 10b-6, 10b-7, and 10b-8 under the Securities Exchange Act of 1934 for Distributions of Foreign Securities to Qualified Institutional Buyers, Sec. Act Rel. No. 33-7028, [1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,249, at 84,658 (Nov. 3, 1993) [hereinafter Release 7028]; Changes to Methods of Determining Holding Period of Restricted Securities Under Rule 144 and 145, Sec. Act Rel. No. 33-6862, [1989-1990 Transfer Binder], Fed. Sec. L. Rep. (CCH) ¶ 84,523, at 80,639, n. 18 (Apr. 23, 1990).

280. *E.g.*, British Airways PLC., SEC No-Action Letter, [1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 76,653 (May 19, 1993); Exemption Regarding Application of Cooling-Off Period Under Rule 10b-6 to Distribution of Foreign Securities, Exchange Act Rel. No. 34-31943, [1992-1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,117 (Mar. 4, 1993); International Stock Exchange of the U.K. and the Republic of Ireland Ltd., SEC No-Action Letter, [1987-1988 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 78,713 (Sep. 9, 1987); Order of Exemptions from Provisions of Rule 10b-6 and 10b-13 under the Securities Exchange Act of 1934 for Canadian Multijurisdictional Disclosure System, Exchange Act Rel. No. 34-29355, [1991 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,813 (June 21, 1991).

281. Release 7028, *supra* note 279, at Rule 10b-6(i).

282. Securities are eligible under this provision if they were not, when issued, of the same class as securities listed on a national securities exchange or quoted in a U.S. automated inter-dealer quotation system. 17 C.F.R. § 230.144A(d)(3) (1995) [hereinafter Rule 144A].

283. *Id.* at (a)(1) (defining "qualified institutional buyer").

284. Securities Act of 1933 § 4(2); 15 U.S.C.A. § 77d(2) (1981).

285. 17 C.F.R. § 230.501-508 (1995) [hereinafter Regulation D].

286. Rule 10b-6(i), *supra* note 272.

287. *Id.*

288. Release 7028, *supra* note 279, at 84,659.

empt market activities worldwide, even if foreign sales are made to non-QIBs. Nonetheless, the exception provided by Rule 10b-6(i) only covers Rule 144A-eligible securities, irrespective of the market in which they are sold and, since securities listed on a national stock exchange or quoted in NASDAQ are ineligible for Rule 144A,[289] "the Commission expects that transactions effected in the United States pursuant to [the new rules] will be limited."[290]

C. *Class Exemptions*

Building upon a class exemption recently granted[291] with respect to sales of certain German securities, in November 1993 the Commission published a Statement of Policy ("Policy Statement") announcing its position on the grant of class exemptions from the Trading Practices Rules in the future relating to issuers from other foreign countries.[292] The overall purpose the Policy Statement is to facilitate distributions of foreign securities in the United States.[293] Prior to the publication of the Policy Statement, the Division of Market Regulation ("Division"), acting pursuant to delegated authority, granted an exemption ("Germany Exemption") from the Trading Practices Rules to distribution participants and affiliated purchasers for transactions outside the United States in actively traded securities ("Qualified German Securities")[294] of highly capitalized German issuers (or certain related securities, "Relevant Securities"),[295] subject to certain conditions.[296] Pursuant to the Germany Exemption, transactions effected in Germany are exempt from the Trading Practices Rules if carried out in accordance with the prescribed terms and conditions, while transactions in the United States must comply with the Trading Practices Rules. Transactions in "Significant Markets," as defined (generally, a securities market in a single country other than the U.S. or Germany with ten percent or more aggregate worldwide trading volume), must be carried out in conformity with the Trading Practices Rules, with cer-

289. Rule 144A, *supra* note 282.

290. Release 7028, *supra* note 279, at 84,659 n. 15.

291. Exemptions from Rules 10b-6, 10b-7, and 10b-8 During Distributions of Certain German Securities, Sec. Act Rel. No. 33-7021, [1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,233 (Oct. 6, 1993) [hereinafter Release 7021].

292. Release 7027, *supra* note 278.

293. *Id.*

294. In order to constitute a "Qualified German Security", a security must: (1) be issued by a foreign private issuer incorporated under German law or a subsidiary thereof, and (2) be a DAX (German stock market index) component security or meet certain quantitative tests based upon average daily trading volume (certain related securities, such as convertibles, also qualify). Release 7021, *supra* note 291, at 84,533.

295. "Relevant Security" is a "Qualified German Security" or a security of the same class and series as, or a right to purchase, a Qualified German Security.

296. Release 7021, *supra* note 291, at 84,533.

tain exceptions.[297]2

The Policy Statement establishes a similar framework for the grant of class exemptions with respect to issuers from other countries. The Commission reasons that by limiting the exemptions from the Trading Practices Rules to actively traded securities of highly capitalized issuers, requiring disclosure in the U.S. market and assuring its own access to transaction information, "the risks of potential manipulative effects from transactions in the principal foreign market substantially are diminished . . . ."[298] The Policy Statement does not actually grant other class exemptions but rather clarifies the circumstances under which they may be granted in the future. Transactions effected in the United States are subject to the Trading Practices Rules, absent another exemption.[299]

Drawing upon the Germany Exemption, the Policy Statement sets forth criteria the Division will examine in determining whether to grant a class exemption. "Persons interested in obtaining a class exemption" must apply in writing to the Division.[300] As part of the application, distribution participants should agree to notify the staff that they will rely upon the exemption.[301] The applicant must propose a category of issuers to which the exemption, if granted, will apply. "A security that is a component of a widely-recognized stock index, and has a market capitalization that is the equivalent of US $1 billion and a value of average daily trading volume of the equivalent of US $5 million, generally would qualify for the exemption."[302] Another element of the exemption is a description of the disclosure that would be included in the U.S. offering documents.[303] The Commission advises that offering documents used in the United States should contain complete disclosure concerning market transactions that may occur in the home country.[304] Further, distribution participants should effect all principal transactions on (or report them to) a "foreign financial regulatory authority" ("FFRA").[305] Distribution participants should agree to report transaction information during the distribution to an independent entity, normally an FFRA in the country in question, and such entity should agree to pass such information along to the Division upon request.[306]

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297. *Id.* at 84,535-36.

298. Release 7027, *supra* note 278, at 84,655.

299. *Id.* at 84,655.

300. *Id.* at 84,655-56.

301. *Id.* at 84,656. The offering coordinator (*e.g.*, lead underwriter) may furnish the notice on behalf of other distribution participants. *Id.*

302. *Id.*

303. *Id.*

304. *Id.*

305. *Id.* For the definition of foreign financial regulatory authority, *see* Section 3(a)(51) of the Exchange Act.

306. *Id.* at 84,657 (the Policy Statement discusses related recordkeeping and re-

In terms of assessing the structure and scope of future class exemptions, the Germany Exemption is instructive. Counsel to Deutsche Bank wrote the SEC concerning "possible offerings of equity securities of certain German companies involving a distribution of some or all of the securities in the United States."[307] Deutsche Bank proceeded to detail the adverse consequences of an extraterritorial application of Rule 10b-6: "the market in Germany for the shares of the company in question could simply collapse . . . , given the high proportion of trading in the shares that is conducted by the larger German banks, and the likelihood that most (if not all) of such banks would act as distribution participants in an offering by a blue-chip German company."[308] The Commission granted the exemption.[309] It is understood, from discussions with the staff, that any person — even those not connected to the person filing the exemptive request — may rely upon the Germany Exemption if the terms of it are satisfied. Presumably, the same result would apply to other exemptions granted pursuant to the Policy Statement.

VI. FINANCIAL SERVICES IN THE EUROPEAN UNION

A. *Investment Services*

In May 1993 the Council, at long last, adopted the controversial directive on investment services.[310] The directive as adopted was based upon a February 1990 proposal by the European Commission.[311] Although the EU had planned for the new investment services regime to become effective simultaneously with the new banking program on January 1, 1993,[312] this goal proved unrealistic. One of

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porting requirements.).

307. Release 7021, *supra* note 291, at 84,520. The request did not apply to straight debt securities. *Id.* at n.1.

308. *Id.* at 84,525.

309. *Id.* at 84,533. The Exemption applies to transactions in Relevant Securities. As indicated, transactions in "Significant Markets," as defined, must be made in accordance with the Trading Practices Rules, with certain exceptions.

310. Council Directive 93/22, 1993 O.J. (L 141/27) [hereinafter Investment Services Directive].

311. Amended Proposal for a Council Directive on Investment Services in the Securities Field, 1990 O.J. (C 42) 7.

312. Member states were required to implement the Second Banking Directive by January 1, 1993. Council Directive 89/646, 1989 O.J., and amending Directive 77/780, 1989 O.J. (L386) 1 [hereinafter Second Banking Directive]. This directive establishes a single license applicable throughout the EEU for the provision of banking and other financial services. Thus, a credit institution is able to provide a wide variety of financial services throughout the EEU. The Second Banking Directive depends upon home state supervision and mutual recognition. On the basis of these principles, "credit institutions" are entitled to engage in, on a community-wide basis, any or all of the following activities, provided that such activities are covered by the home state authorization: acceptance of deposits from the public; lending; trading

the purposes of the Investment Services Directive was to ensure that non-banks not covered by the Second Banking Directive were not put at an unfair competitive disadvantage in relation to banks which had the benefit of the European passport.[313] Nonetheless, since the Second Banking Directive, by and large, has already been implemented, credit institutions do have an advantage over non-banks inasmuch as the former have the benefit of the European passport as of January 1993[314] whereas national legislation to implement the ISD need not be effective until December 31, 1995.[315]

Prior to the 1993 adoption of the ISD, the European Commission engaged in a heated debate over its terms.[316] One group of member states, led by France, supported an amendment to the Investment Services Directive to restrict investment firms from engaging in "off-

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transferable securities, money market instruments, options and futures, foreign exchange, and exchange and interest rate instruments; providing investment and financial advisory services; participating in stock issues and providing services related to such issues. *Id.* at Preamble, Annex, and art. 18. Other activities credit institutions may engage in on a community-wide basis include financial leasing; money transmission services; issuing and administering means of payment (*e.g.*, bankers' drafts); issuing guarantees and commitments; money brokering; safekeeping and safe custody services; and credit reference services. *Id.*, Annex. Banks may engage in other activities (*i.e.*, those not included in the Annex) to the extent permitted by the Treaty of Rome. Second Banking Directive, *supra*, Preamble. A credit institution may only engage in the activities that are covered by its authorization from its home country. Banks operating under the Second Banking Directive may provide all such services, including investment services, authorized by the home member state, without obtaining an additional license under the Investment Services Directive. Banks providing investment services in member states would be subject, however, to other provisions of the Investment Services Directive. Articles 2, no. 4; 8, no. 2; 10 (prudential rules adopted by home state); 11 (host state rules of conduct); 12 (first paragraph); 14, nos. 3 (transactions on regulated markets) and 4 (opt out of same); 15 (access to regulated markets including stock exchanges); 19 and 20 of the Investment Services Directive apply to investment firms that are credit institutions authorized by their banking license to render investment services. *See* art. 2, no. 1. It is expected that competition among EU states will lead to wide acceptance of "universal" (combined commercial and investment) banking.

313. THE SECURITIES ASSOCIATION, INVESTMENT SERVICES DIRECTIVE: A COMMENTARY AND ANALYSIS, 16 (March 1989) [hereinafter SECURITIES ASSOCIATION].

314. It may be possible to mitigate the effect of this regulatory disadvantage through the use of affiliate corporations. For example, investment firms may find it desirable to form a banking subsidiary in an EU country. *Developments on the Capital Adequacy Directive*, FIN. REG. REP., Nov. 18, 1991, at 235. Also, securities firms which are 90 percent owned subsidiaries of banks may have the ability to provide Community-wide services, including investment banking services, by virtue of the banking licenses of their parents, inasmuch as the Second Banking Directive extends the banking passport to 90 percent owned subsidiaries in certain cases. David Barnard, *Developments in the European Community and the United Kingdom*, in INT'L SECURITIES MARKETS 181, 193 n. 42 (743 PLI 1991) [hereinafter Barnard I]; Second Banking Directive, *supra* note 312, at art. 18(2).

315. Investment Services Directive, *supra* note 310, at art. 31.

316. London, *AIBD Opposes Plan to Amend EC Directive*, FIN. TIMES, Feb. 28, 1991, at 30.

exchange" trading.[317] Other countries, such as Britain and Germany, strenuously opposed France's initiative which they viewed as inconsistent with their loosely regulated off-exchange markets.[318] The ISD, as adopted in 1993, allows member states to require transactions to be carried out on a "regulated market."[319] However, in this event member states must give residents the right (subject to certain conditions) not to comply with the requirement "and have the transactions carried out away from a regulated market."[320] Another issue contributing to the impasse over the ISD was the issue of transparency — the extent to which trade information must be disclosed to the public and the timing of such disclosure. The matter was resolved in 1993 by adopting minimum standards but leaving considerable discretion to the regulatory authorities of each member state.[321]

The Investment Services Directive provides for a home state license that will allow investment firms to provide in any member state the investment services that are authorized by the home member state.[322] An investment firm will be able to provide investment ser-

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317. *Pan-European Share Markets: More Matter, Less Art*, ECONOMIST, Dec. 8, 1990, at 86; *Finance Ministers Deadlocked On Off-Exchange Trading Regulations*, INT'L SEC. REG. REP. (BNA) 6 (Dec. 1990); *Off-Exchange Trade Compromise Unlikely to Succeed*, INT'L SEC. REG. REP. (BNA) 4 (Jan. 14, 1991).

318. *Id.*; Clarkson, *EC States Continue War Over Investment Regime*, REUTERS, Dec. 14, 1990.

319. Investment Services Directive, *supra* note 310, at art. 14, no. 3.

320. *Id.* at art. 14, no. 4. "Member States may make the exercise of this right subject to express authorization, taking into account investors' differing needs for protection and in particular the ability of professional and institutional investors to act in their own best interests." *Id.* Prior to adoption of the ISD, a commentator observed that "[p]ractitioners in the Eurobond markets are . . . concerned that the ability to opt out may be hedged around with restrictions, and would like to see a specific exemption from the so called 'concentration' provisions for Eurosecurities." David Barnard, *The Evolving Pace of Regulation of The Financial Services Industry in the European Community*, in INT'L SECURITIES MARKETS 212 (PLI 1993) [hereinafter Barnard II].

321. Investment Services Directive, *supra* note 310, at art. 21. The U.S. has almost immediate reporting of trade data for reported securities on the consolidated tape. Roberta Karmel, *The Stalled Investment Services Directive*, N.Y.L.J., June 18, 1992, at 1, 3.

322. Investment Services Directive, *supra* note 310, at art. 3 and 12. An "investment firm" is any legal (as opposed to natural) person whose regular occupation or business is to provide any "investment service." *Id.* at art. 1, no. 2. Member states may consider natural persons to be "investment firms" under certain circumstances. *Id.* One commentator points out that there has been a "continuing debate over whether the single license should be granted to 'natural persons' as opposed to investment firms. Some member states worry that it may be impossible to separate the capital of the business from that of the owner. However, the counter-argument is that to discriminate against natural persons is contrary to the spirit of the EC Treaty." Barnard II, *supra* note 320, at 233 n. 67. "Investment service" is defined below. The 'home member state' is the member state where the investment firm has its registered office, or its head office if it does not have a registered office. Investment Services Directive, *supra* note 310, at art. 1 n. 6. If the investment firm

vices directly or by establishing a branch in another member state.[323] The following are "services" encompassed within the directive: receiving and transmitting, on behalf of investors, orders for securities (and other specified instruments); dealing in such securities or instruments for the firm's own account; portfolio management; and underwriting or placements.[324] The investment firm may render only those services specified in its authorization. If an investment firm is licensed to render any of the services indicated above (*i.e.*, those referenced in Annex A to the ISD), the home state may also authorize the firm to provide certain "non-core services" (*i.e.*, those specified in Annex C to the ISD).[325] The investment firm may provide the foregoing services with respect to: transferable securities; units in undertakings for collective investment in transferable securities; money market instruments; financial futures contracts, including cash-settled instruments; forward interest-rate agreements; interest rate, currency and equity swaps; and options on any of the foregoing, including options on currency and interest rates.[326] A controversial provision requires host

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is a natural person, the home member state is the member state where that person's head office is situated.

323. Investment Services Directive, supra note 310, at art. 14 n. 1. The procedures for establishing a branch and for providing services are set forth in Article 17 and 18, respectively. In Dec. 1990, Italy passed securities legislation which introduced a new financial intermediary, *see Italy Reforms Securities Market*, DOING BUSINESS IN EUROPE , Jan. 14, 1991, at 1. and enacted secondary legislation in July 1991. The new legislation requires any firm desiring to render securities business in Italy to act through a locally incorporated subsidiary. The U.K. government among others complained to the EU on grounds that the requirement to conduct securities business through a subsidiary violates the Treaty of Rome. *Italy, United Kingdom: UK Government Complains to EC about Italian Securities Law*, DOING BUSINESS IN EUROPE, Jan. 14, 1991, at 865.

324. The exact language of the directive should be consulted concerning the services which may be rendered. Investment Services Directive, *supra* note 310, at Annex, Section A.

325. *Id.* at art. 3, no. 1. The non-core services include custodial, safekeeping and administrative services with respect to securities and other specified financial instruments; extending margin under certain circumstances; financial, investment and M&A advice; services related to underwriting; and foreign exchange services related to investment services. For the precise non-core services, *see Id.* at Annex, Section C. Authorization within the meaning of this Directive may in no case be granted for services covered only by Section C of the Annex. *Id.* at art. 3, n. 1.

326. *Id* at Section B. As stated above, pursuant to the Second Banking Directive, credit institutions will be able, among other things, to trade securities and participate in stock issues on the basis of their banking license, if authorized by the home state. A bank may provide these services on the basis of its banking license (if covered in its authorization) without obtaining additional authorization under the Investment Services Directive. *Opinion on the Proposal for a Council Directive on Investment Services in the Securities Field*, 32 O.J. EUR. COMM. (No. C 298) 6, 9 (1989); Lobl and Werner, *1992 Effects on Securities Regulation and Mergers and Acquisitions in the European Community*, 21 ANN. INST. ON SEC. REG. 9, 16 (1989). Thus, for example, a German bank which was authorized by the banking authorities to engage in securities business would not also be required to be authorized by a securities regulator. Securities Association, *supra* note 311, at 17. Certain provisions

member states to grant access by investment firms from other member states to membership of stock exchanges and "regulated markets" in their country.[327] This provision applies to banks as well as non-bank investment firms,[328] although there is a transition provision for banks.[329] The provision also applies to regulated markets that operate without a physical presence.[330] "Member states shall abolish any national rules or laws or rules of regulated markets which limit the number of persons allowed access thereto."[331] Investment firms must have the choice of becoming members of regulated markets or having access thereto either directly, by setting up branches in the host state, or indirectly, through subsidiaries or acquisitions.[332]

Investment firms are required to be authorized by their home state but not the host state prior to providing investment services.[333] To obtain home state authorization, a person must apply to the home state, furnish a plan of operations, satisfy capital requirements,[334]

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of the Investment Services Directive would apply to such activities, however. Investment Services Directive, *supra* note 310, at art. 2, No. 1. For example, the "prudential" rules of the Investment Services Directive would apply to all institutions doing securities business, whether banks or non-banks. ISD, art. 2, no. 1, art. 10. *See also Id.* at art. 11 (conduct of business); SECURITIES ASSOCIATION, *supra* note 313, at 18.

327. Investment Services Directive, *supra* note 310, at art. 15. The right of access applies when investment firms are authorized for brokerage (execution of orders other than for own account) and dealing (dealing for own account). *Id.* The host state must also ensure that such investment firms have access to membership of clearing and settlement systems of the host state exchanges or markets which are available to members of such exchanges and markets. *Id.* A "regulated market" is a market for securities or certain other financial instruments that is so designated by the home state, functions regularly, and is regulated as described in Article 1, no. 13. *Id.* at art. 1.

328. *Id.* at art. 2. Article 15 (among others) applies to credit institutions the authorization of which covers one or more of the investment services listed in Section A of the Annex. *Id.* at art. 2, no.1. *See generally* Kellaway, *EC Investment Market Plan Hits Trouble*, FIN. TIMES, Nov. 20, 1990, at 3. Stock exchanges in some countries do not allow banks to join as members except through a separate securities subsidiary. *Developments on the Capital Adequacy Directive*, FIN. REG. REP., Nov. 18, 1991, at 320. The resolution of the issue in the ISD as adopted "will result in a major change for some EC countries and it will be interesting to see whether it will result in major over-capacity in some markets, as in the UK after Big Bang and the deregulation of the London Stock Exchange." Barnard II, *supra* note 320, at 213.

329. Investment Services Directive, *supra* note 310, at art. 15, no. 3. States that, at the time the ISD was adopted, do not grant banks direct access to stock exchanges or other regulated markets may continue to require access only through "specialized subsidiaries" until the end of 1996. *Id.* Spain, Greece and Portugal may extend the period until the end of 1999. *Id.*

330. *Id.* at art. 15, n. 4.

331. *Id.* at art. 15, n. 1. "If, by virtue of its legal structure or its technical capacity, access to a regulated market is limited, the Member State concerned shall ensure that its structure and capacity are regularly adjusted." *Id.*

332. *Id.* at art. 15, n. 2.

333. Investment Services Directive, *supra* note 310, at art. 3.

334. Capital requirements that will be applicable to investment firms are treated

and disclose the names of principal owners who must satisfy home state suitability requirements.[335] While the directive allows member states to license subsidiaries of companies governed by the law of non-EU countries, it establishes a procedure similar to that of the Second Banking Directive for monitoring the treatment of EU investment firms in third countries.[336] Member states, subject to review by the Council, may limit or suspend the licensing of firms from third countries, except for the establishment of subsidiaries by investment firms already authorized in the EU or the acquisition of shares of EU firms by such previously authorized firms.[337] The Investment Services Directive expressly allows member states to license subsidiaries of companies governed by the law of non-EU countries. Member states may not apply to branches of non-EU investment firms provisions that result in more favorable treatment than that accorded to branches of member state investment firms.[338]

The directive requires compliance with the initial and other capital requirements of the Capital Adequacy Directive.[339] Like the Bank Directive, the Investment Services Directive grants primary supervisory responsibility over an investment firm to the home country. The directive requires home member states to adopt "prudential" rules which investment firms "shall observe at all times."[340] These "prudential rules" must govern the following aspects of investment firms' business, among others: administrative and accounting procedures and internal control; safeguarding investors' funds and securities; record-keeping; and conflicts of interest.[341] It was expected that, at least initially, the EU would continue to allow the host state to regulate some aspects of investment firms' business (*e.g.*, conduct of business, advertising).[342] There have been suggestions that "conduct of business" rules eventually would be the subject of another EU directive.[343] As adopted in 1993, the Investment Services Directive requires member states to promulgate rules of conduct applicable to investment firms.[344] "Without prejudice to any decisions to be taken in the context of the harmonization of the rules of conduct, their implementation

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in the Capital Adequacy Directive.

335. Investment Services Directive, *supra* note 310, at art. 3 and 4.

336. *Id.* at art. 7. *See* Levintin, *The Treatment of United States Financial Services Firms in Post-1992 Europe*, 31 HARV. INT'L L. J. 515 (1990).

337. Investment Services Directive, *supra* note 310, at art. 7, no. 5.

338. *Id.* at art. 5.

339. *Id.* at art. 8.

340. *Id.* at art. 10.

341. *Id. See also Id.* at art. 12 concerning compensation (insurance) funds for the protection of investors.

342. Appel, *EEC-1992 and the Securities Industry*, 23 REV. SEC. & COMM. REG., Apr. 11, 1990, at 70.

343. Lobl and Warner, *supra* note 327, at 17; *New Directive Underway on Capital*, Market Risk, INT'L SEC. REG. REP., June 7, 1989, at 9.

344. Investment Services Directive, *supra* note 310, at art. 11.

and the supervision of compliance with them shall remain the responsibility of the Member State in which a service is provided."[345]

The directive establishes an important grandfathering provisions for investment firms already operating in EU countries.[346] Firms operating with a member state license before the end of 1995 will be deemed licensed for purposes of the ISD if the home state laws require as a condition of engaging in such activities compliance with applicable capitalization and suitability requirements.[347] Member states must, by July 1, 1995, adopt implementing legislation that must become effective no later than December 31, 1995.[348]

B. *Capital Adequacy*

In 1993, the Council, based upon an earlier proposal by the European Commission,[349] adopted a directive ("Capital Adequacy Directive" or "CAD") concerning the capital adequacy of investment firms and credit institutions.[350] Member states are required to apply some of the provisions of the Capital Adequacy Directive to credit institutions as well as investment firms.[351] States may adopt measures more stringent than those required by the directive if they choose.[352] Investment firms must have initial capital of at least ECU 730,000,[353] unless they fall within one of the exceptions set forth in Article 3 of the CAD. Firms engaging only in brokerage or portfolio management, and which (with certain exceptions) do not deal in financial instruments for their own account, or underwrite financial instruments of a firm commitment basis, must have initial capital of at least ECU 125,000.[354] The initial capitalization requirement decreases to ECU 50,000 where the firm is not authorized to hold clients' funds or securities, to deal for its own account or to underwrite issues on a firm commitment basis.[355] These minimum capital requirements do not apply to credit institutions, which are governed in this respect by the capital provisions of banking directives.[356] A grandfathering provision

345. *Id.* at no. 2.

346. *Id.* at art. 30, no.1.

347. *Id.* at art. 30, n. 1, (requiring compliance with conditions equivalent to articles 3(3) (initial capital, reputation of managers) and 4 (suitability of owners)).

348. *Id.* at art. 31.

349. *Proposal for a Council Directive on Capital Adequacy of Investment Firms and Credit Institutions*, COM(90) 141 Final—SYN 257, 1990 O.J. (C 153).

350. Council Directive 93/6, 1993 O.J. (L 141) 1 [hereinafter Capital Adequacy Directive].

351. *Id.* at art. 1 No. 1.

352. *Id.* at art. 1, no. 2.

353. *Id.* at art. 3, n. 3.

354. *Id.* at art. 3, n. 1.

355. *Id.* at art. 3, n. 2.

356. Article 3, by its terms, applies only to "investment firms," the definition of which, in article 2, excludes credit institutions. *See also EC Briefings: Capital Ade-*

is available for firms "in existence before this Directive is applied."[357] In general, an investment firm's capital may not fall below that initially required for authorization.[358]

The Capital Adequacy Directive requires both investment firms *and* credit institutions to maintain a specified amount of capital for risks associated with certain activities, including trading activities.[359] These institutions must provide a specified amount of capital to cover four categories of risk: position risk; counterparty/settlement risk; foreign exchange risk; and large exposures.[360] These risks must be quantified in accordance with the directive, the sum of them constituting the "own funds" (capital) requirement. The capital requirement of investment firms may not be less than the amount prescribed in Annex IV to the CAD (generally, one-quarter of fixed overhead for the preceding year).[361] Member states may choose to allow institutions (banks and investment firms) to calculate capital requirements for trading activities in accordance with the Solvency Ratio Directive[362] rather than Annexes I and II of the CAD under certain circumstances.[363]

VII. INTERNATIONAL ORGANIZATION OF SECURITIES COMMISSIONS

A. *Introduction*

The International Organization of Securities Commissions and Similar Organizations held its 1994 annual meeting in Tokyo but made little tangible progress toward the internationalization of securities regulation. Future annual meetings are scheduled for Paris, 1995 and Montreal, 1996. It had previously appeared that IOSCO might make a significant contribution to the development of capital adequacy standards yet the realization of this goal proved illusory in 1992 and 1993. At present, IOSCO presently serves as the principal forum for the study and discussion on international securities issues but does not have a mandate to adopt binding international principles. In 1993, the President's Committee adopted a resolution calling for members to

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quacy, INT'L FIN. L. REV., June 1990, at 44. Article 8 of the Second Banking Directive requires initial capital of at least ECU 5 million, with certain exceptions. Bank capital requirements in the European Union should be viewed in context of the development of international norms by the Basle Committee of the Bank for International Settlements and the International Organization of Securities Commissions (IOSCO).

357. Capital Adequacy Directive, *supra* note 350, at art. 3, n. 5.

358. *Id.* at art. 3, n. 8.

359. *Id.* at art. 4.

360. *Id.* at Annexes 1-4.

361. *Id.* at art. 4, n. 1.

362. Council Directive 89/647, 1989 O.J. (L. 386) 14.

363. Capital Adequacy Directive, *supra* note 350, at art. 4, n. 6.

accept cash flow statements prepared in accordance with a standard developed by the International Accounting Standards Committee. Subsequently, the SEC decided to allow foreign issuers to use the international standard without a reconciliation to U.S. GAAP.[364]

Despite its American origins, IOSCO has become a truly international organization. The 14th annual conference in Venice was attended by representative from all the major financial centers, including Germany and Japan,[365] and membership has increased steadily since that time. The charter members of IOSCO are the countries of the American continent plus Quebec and Ontario; non-charter members include other countries that have joined the organization. "Affiliate" membership is a category created for self-regulatory organizations.[366] While affiliate members do not have voting privileges and may not attend meetings of the President's Committee or the Executive Committee, they are allowed to be members of the Technical Committee (see below) and its working parties.[367] The category of "associate member" was created to allow participation in the President's Committee and the Technical Committee of organizations of regulators or other government regulators where a country already has a full member.[368] The total number of members (in all categories) in 1993 was

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364. Release 7053, *supra* note 204, at 85,205. The SEC subsequently proposed to accept another international standard relating to business combinations.

365. In 1988, Japan, West Germany, Austria and Turkey joined IOSCO. *See Regulators Agree to Move Cautiously on Enforcement, Accounting Standards*, INT'L SEC. REG. REP., Nov. 11, 1988, at 1. In 1991, IOSCO admitted the following as voting members: Amman, Kenya, Luxembourg and Mauritius. In 1992, IOSCO accepted four new voting members: Bermuda, Ivory Coast, Malta and South Africa. In 1993, IOSCO accepted five new voting members: the Bahrain Stock Exchange; the Central Bank of Ireland; the Securities Commission of Malaysia; the Corporate Law Authority of Pakistan; and the Securities and Exchange Commission of Sri Lanka. *Final Communique of the XVIIth Annual Conference of IOSCO*, Oct. 28, 1993, at 8 [hereinafter *18th Communique*].

366. *IOSCO Sees Major Effort on Futures and Ethics in Chile*, INT'L SEC. REG. REP., July 16, 1990, at 265; *IOSCO Drops Overview of Crash Studies, Will Focus on Working Group Findings*, INT'L SEC. REG. REP., Oct. 12, 1988, at 116.

367. *IOSCO in Chile*, supra note 366. As of July 1990, there were applications for affiliate membership pending from The New York Stock Exchange, Sidney Futures Exchange, Investment Dealers' Association of International Bond Dealers, and the Australian Stock Exchange. *Id.* In 1991 IOSCO admitted the following as affiliate members: Mercado Abierto Electronico of Argentina, Tokyo Stock Exchange, Japan Securities Dealers Association, Oslo Stock Exchange, National Futures Association of the United States, the CBOT and the Options Clearing Corporation of the United States. IOSCO admitted six new affiliate members in 1992: Bolsa de Comercio of Buenas Aires; the Vienna Stock Exchange; Bolsa de Valores de Sao Paulo; the Korea Stock Exchange; the Korea Securities Dealers Association; and the Thailand Stock Exchange. *Final Communique of the XVIIth Annual Conference of the International Organization of Securities Commissions*, Oct. 29, 1992, at 9 [hereinafter 17th *Communique*]. IOSCO accepted three new affiliate members in 1993: The Consiglio di Borsa of Italy, the Taiwan Stock Exchange, and the London International Financial Futures and Options Exchange. *Id.* at 8.

368. *IOSCO in Chile*, supra note 366. In 1988, The U.S. Commodities Futures

110.[369]

The organizational structure of IOSCO includes the General Assembly, a General Secretary (and General Secretariat located at the Quebec Securities Commission,) and various committees. The President's Committee consists of the presidents of all of the member agencies, while the Executive Committee consists of elected members.[370] There are Regional Standing Committees, a Consultative Committee[371] and a Development Committee.[372] The Technical Committee, constituted by the Executive Committee in May 1987, focuses on identifying and solving international regulatory problems, while the Executive Committee administers the affairs of the organization.[373] The Technical Committee consists of representatives from the leading financial centers.[374] This Committee has established a number of Working Parties to concentrate on specific substantive issues. As of October 1993, these subgroups of the Technical Committee included the following Working Parties: (1) multinational disclosure and accounting which has a subgroup on accounting and auditing standards; (2) regulation of secondary markets; (3) regulation of market intermediaries; (4) enforcement and the exchange of information; and (5) investment management, formed in 1993. These Working Parties, and

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Trading Commission and the Association of Swiss Stock Exchanges were admitted as Associate Members. *Regulators Agree to Move Cautiously on Enforcement, Accounting Standards*, INT'L SEC. REG. REP., Nov. 23, 1988, at 134. The British Columbia Securities Commission and the North American Securities Administrators Association are also Associate Members. *IOSCO in Chile*, *supra* note 366. In 1992 IOSCO accepted the Financial Supervision Commission of the Isle of Man; the Financial Services Department of the States of Jersey and the Stock Exchange Commission of the Zurich Cantonal Department of Economics as Associate Members in 1992. 17th *Communique*, *supra* note 367, at 9. The Securities and Exchange Surveillance Commission of Japan became an associate member in 1993.

369. 18th *Communique*, *supra note* 365, at 8.

370. 17th *Communique*, *supra* note 367, at 1. Regional Committees and the Development Committee are also represented on the Executive Committee.

371. The Consultative Committee, which "provides specialized worldwide input into the organization," *IOSCO Officials Meet to Map Out Harmonization Effort*, INT'L SEC. REG. REP., Dec. 6, 1990, at 1, was established in 1988 and is composed of global self-regulatory organizations. *IOSCO in Chile*, *supra* note 366.

372. *See Harmony and Wariness Coexist at IOSCO's Conference in Venice*, INT'L SEC. REG. REP., Sept. 27, 1989, at 1. The purpose of the Development Committee is to promote the development of emerging markets, "in particular the exchange of information and the implementation of common standards." 17th *Communique*, *supra* note 367, at 5. The Development Committee has the following six working groups: Working Group on Clearing and Settlement; Working Group on Internationalization; Working Group on Disclosure; Working Group on Institutional Investors; Working Group on Privatization; and Working Group on Derivatives.

373. *IOSCO Drops Overview of Crash Studies, Will Focus on Working Group Findings*, INT'L SEC. REG. REP., Oct. 12, 1988, at 213, 216.

374. As of 1993, the Technical Committee included representatives from Australia, France, Germany, Hong Kong, Italy, Japan, the Netherlands, Mexico, Ontario, Quebec, Spain, Sweden, Switzerland, the United Kingdom and the United States.

the substantive issues they are addressing, are discussed below.

B. *Substantive Agenda*

1. Disclosure and Accounting

IOSCO's substantive agenda consists primarily of eight substantive items,[375] one of which is the harmonization of requirements applicable in the case of multinational offerings. The Working Party studying this area started its inquiry with the empirical question of why offerings were not made in certain jurisdictions despite investor interest in the offering.[376] The Working Party's report relating to multinational equity offerings was adopted at IOSCO's 14th annual meeting.[377] The report, recommending development of a regime that would allow use of a single disclosure document in multijurisdictional offerings,[378] discussed two principal avenues for reaching the goal of a single prospectus, namely: (i) harmonization of disclosure standards, and (ii) reciprocity (acceptance of home country or predominant market requirements).[379] The report also urged the development of internationally accepted accounting and auditing standards upon which a universal disclosure document could be based.[380] Finally, the report recommended the coordination of national timetables for securities offerings, as well as a study of periodic information that could be used as the basis for a new issue prospectus; a study of the proper role of stabilization practices; a study of greater standardization in the area of resales of privately placed securities; and an annual survey of regulatory changes in financial centers that could affect multinational offerings.[381] During the 16th Annual Conference, the Technical Committee released a report entitled *Comparative Analysis of Disclosure Regimes* and study entitled *A Status Report on International Accounting and Auditing Standards*. The final communique for the 17th Annual Meeting states that the objective of the Working Party on Multinational Disclosure and Accounting is, "so far as is consistent with maintaining

375. International Equity Offerings; Accounting and Auditing; Capital Adequacy; Off-Market Trading; Memoranda of Understanding; Clearance and Settlement; Futures Market Regulation; and Ethics.

376. *Regulators Agree to Move Cautiously on Enforcement, Accounting Standards*, INT'L SEC. REG. REP., Nov. 23, 1988, at 1.

377. *Harmonization and Wariness Coexist at IOSCO's Conference in Venice*, INT'L SEC. REG. REP., Sept. 27, 1989, at 1.

378. Roberta Karmel, *The IOSCO Venice Conference*, N.Y.L.J., Oct. 19, 1989, at 16.

379. *Technical Committee Issues Disclosure Recommendations*, INT'L SEC. REG. REP., Sept. 27, 1989, at 4.

380. *Ruder Says IOSCO Report Offers Blueprint for Global Offerings*, INT'L SEC. REG. REP., Sept. 27, 1989, at 10.

381. Karmel, *supra* note 378; *Technical Committee Issues Disclosure Regulations*, INT'L SEC. REG. REP., Sept. 27, 1990, at 11.

the quality of regulation necessary for the protection of investors, to actively promote regulation which facilitates the process whereby world class issuers can raise capital in the most cost effective and efficient way in all capital markets where investor demand exists."[382] The final communique for the 18th annual meeting reiterated this proposition, except that it deleted the term "world class."[383]

At the 13th annual meeting, IOSCO refused to endorse the recommendation of a workshop that called for the adoption of common international accounting and auditing standards.[384] Yet at the following annual meeting, the Secretary General of IOSCO stated, over optimistically, "'we expect to complete the process of writing international standards for securities industry accounting and auditing by 1992.'"[385] The European Communities have, of course, been working on their own accounting standards, and IOSCO realized that the adoption of standards by the EC that differ from those ultimately endorsed by IOSCO could destroy the hope of an internationally acceptable standard.[386] By 1992, the Working Party on Multinational Disclosure and Accounting had completed a review of the auditing standards of the International Auditing Standards Committee (IAPC) and called for recognition of such standards by the international community. The Presidents Committee of IOSCO adopted a resolution to this effect, urging members of IOSCO to recognize International Accounting Standards ("IASs") for use in cross-border offerings and continuous reporting by foreign issuers.[387] The Working Party has been involved in an analysis of accounting standards developed by the International Accounting Standards Committee.[388] In 1993, the President's Committee resolved that members take all necessary steps to accept cash flow statements prepared in accordance with IAS 7 as an alternative to domestic standards in connection with cross-border offerings and reporting by foreign issues.[389] As part of a recent rule-making action, the SEC, taking its cue from IOSCO, decided to accept cash flow statements prepared in accordance with International Accounting Standard No. 7, without a reconciliation to U.S. GAAP.[390]

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382. 17th *Communique*, *supra* note 367, at 2.

383. 18th *Communique*, *supra* note 365, at 2.

384. *Regulators Agree to Move Cautiously on Enforcement, Accounting Issues*, INT'L SEC. REG. REP., Nov. 23, 1988, at 1.

385. *Harmony and Wariness Coexist at IOSCO's Conference in Venice*, INT'L SEC. REG. REP., Sept. 27, 1989, at 56.

386. *See IOSCO: EC Moves Could Doom Global Accounting Harmony*, INT'L SEC. REG. REP., Jan. 17, 1990, at 6.

387. 17th *Communique*, *supra* note 367, at 3. *See also Auditing Standards Win Approval From IOSCO for Multinational Reporting*, SEC. REG. L. REP., Nov. 6, 1992, at 1730. The full membership of IOSCO also passed a resolution urging recognition of international auditing standards. *Id.* These resolutions do not address the questions of auditor qualifications and independence. *Id.*

388. *Id.*

389. 18th *Communique*, *supra* note 365, at 3.

390. Simplification of Registration and Reporting Requirements for Foreign Com-

2. Regulation of Secondary Markets

The Working Party on the Regulation of Secondary Markets has been engaged primarily in a study of the relationship between cash and derivative markets for equities.[391] In 1992, IOSCO released a report entitled *Report on Contract Design of Derivative Products on Stock Indices and Measures to Minimize Market Disruption*.[392] A Report entitled *Mechanisms to Exchange Open and Timely Communication Between Market Authorities on Related Cash and Derivative Markets During Periods of Market Disruption* was released at the 1993 meeting. This Working Party also prepared a report on so-called market "transparency" (disclosure of trade information) and will be considering the feasibility of developing minimum international transparency standards.[393]

3. Regulation of Market Intermediaries

In the early 1990s, IOSCO accelerated its effort to coordinate its positions on capital adequacy with other international regulatory authorities. Toward this end IOSCO, at the 16th Annual Meeting, decided to send a memorandum concerning its views on capital adequacy to the Basle Committee of Banking Supervision,[394] and thereafter had several meetings with the Basle Committee.[395] IOSCO announced, in 1992, that it "welcomed" the opportunity to hold further discussions with the Basle Committee concerning "the use of subordinated loans and the trading book versus the investment account."[396] In 1992, the President's Committee adopted "Principles Governing the Supervision of Financial Conglomerates."[397]

In the memorandum to the Basle Committee, the Technical Committee stated that it was willing to conclude an agreement with Basle designed to establish an international standard for market risk re-

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panies; Safe Harbors for Public Announcements of Unregistered Offerings and Broker-Dealer Research Reports, Sec. Act Rel. No. 33-7029, [1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,252 (Nov. 3, 1993).

391. 17th *Communique*, *supra* note 367, at 3.

392. *Id.*

393. *Id.*

394. The Basle Committee on Banking Supervision is an advisory body engaged in an effort to develop rules for regulation of international banking. GAO, SECURITIES MARKETS: CHALLENGES TO HARMONIZING INTERNATIONAL CAPITAL STANDARDS REMAIN 35 (1992). The Committee adopted the so-called Basle Accord in 1988 which its members regard as binding although it is not enforceable as a treaty. *Id.*

395. *Bank, Stock Regulators Near Agreement on Global Capital Levels for Securities*, SEC. REG. L. REP., Feb. 7, 1992, at 170; *Breeden and Corrigan Issue Statement on International Capital Standards*, 92-23 THE SEC TODAY, Feb. 4, 1992, at 1.

396. 17th *Communique*, *supra* note 367, at 4.

397. *Id. See also* Ralph Aldwinckle, *The Regulation of International Financial Conglomerates* (Oct. 29, 1992) (paper presented at 17th Annual IOSCO Conference).

quirements and a definition of permitted regulatory capital.[398] IOSCO envisioned an agreement that would establish minimum levels of market risk requirements for internationally active securities intermediaries.[399] One of the principal purposes of IOSCO's overture toward Basle was its recognition that as internationally active banks become increasingly involved in securities activities, the old regulatory dichotomies between banks and securities firms tend to become obsolete.[400] The Technical Committee indicated in its memorandum to Basle that it would be willing to adopt a "building block" approach to capital adequacy which carved out specific risk requirements from those applicable to general market risk.[401] The Technical Committee would support the building block approach with respect to market risk requirements for debt securities.[402] The SEC indicated it would not oppose this approach as a minimum standard but would retain its current net capital rule for equities which would require a higher standard.[403] "There are differences of view about the acceptability of the building block approach as regards equity securities,"[404] but the Technical Committee recommended that in any event the international community should work out an internationally acceptable minimum capital standard relating to trading in equity securities.[405] For the "sake of convergence," a majority of the Technical Committee indicated at the 16th Annual Meeting that it could accept a minimum standard for highly liquid equities of four percent of capital on gross positions and eight percent of capital on net positions (netting long and short positions).[406] The memorandum to the Basle Committee also sets forth the Technical Committee's views on the use of subordinated regulatory loan capital by securities firms.

At a subsequent meeting of the Technical Committee, then SEC Chairman Breeden reportedly angered other committee members by

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398. *Final Communique of the XVI Conference of the International Organization of Securities Commissions*, Sept. 26, 1991, at Appendix A [hereinafter 16th *Communique*].

399. *Id.*

400. *Id.*

401. *Id.* Most countries have a single capital standard and do not use the building block approach which requires separate calculations for gross and net positions. *Securities Regulation*, ECONOMIST, Oct. 5, 1991, at 177.

402. 16th *Communique*, *supra* note 398.

403. The SEC's approach is referred to as the "comprehensive approach" pursuant to which the capital requirement is a percentage of the portfolio. *See Technical Committee Sends Capital Memorandum to Banking Supervisors*, INT'L SEC. REG. REP., Oct. 7, 1991, at 4. The building block approach treats market and credit risk separately. *Id.*

404. 16th *Communique*, *supra* note 398, at Appendix A.

405. *The 1991 IOSCO Conference*, FIN. REG. REP., Oct. 1991, at 245.

406. 16th *Communique*, *supra* note 398, at Appendix A; *Securities Regulation supra*, note 401. (For equities that are not "highly liquid," the requirement suggested was eight percent and eight percent as opposed to four percent and eight percent.)

indicating opposition to the building block approach, in favor of the "comprehensive" approach.[407] At the 1992 Annual Meeting in London, Breeden opposed several aspects of IOSCO's proposed capital standard,[408] in particular the appropriate level of capital to cover risks of loss on equity securities. The principal issue involves the extent of capital that should be required in the case of long positions in equities hedged by short positions.[409] According to the *Financial Times*, "Mr Breeden . . . insists that long and short positions in equities are not perfect hedges, and can leave securities firms with substantial exposure."[410] Mr. Breeden also reportedly allowed that the EU's capital requirements, which are similar to those proposed by IOSCO, are "highly unsafe,"[411] a pronouncement that, not surprisingly, drew fire from EU spokesmen.[412] By the end of the 1992 Annual Meeting the issue of capital adequacy remained unresolved,[413] and substantial progress is not expected in the short term.

4. Enforcement and the Exchange of Information

In 1992, the Working Party on Enforcement and the Exchange of Information completed a report on money laundering designed to facilitate measures in member countries to curb money laundering through securities and futures markets. This Working Party is also studying "boiler-room operations" and will be examining "the enforcement issues raised by screen-based trading."[414] In 1991, the President's Committee released "Principles for Memoranda of Understanding." The President's Committee adopted a resolution in 1993 concerning transnational retail securities and futures fraud.

5. Investment Management

In 1992, IOSCO announced it was considering forming a Working Party concerning the field of investment management.[415] The Work-

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407. *Disagreement Plagues Committee Discussions on Harmonized International Capital Standards*, INT'L SEC. REG. REP., July 17, 1992, at 238. Again, under the comprehensive approach a percentage of the portfolio serves as the capital requirement, whereas the building block approach "allows securities firms to offset their long and short positions." *Id.*

408. Weston and Corrigan, *Breeden Opposes IOSCO Capital Standard*, FIN. TIMES, Oct. 28, 1992, at 19.

409. *Hopes Dwindle for New Agreement on Capital Requirements*, FIN. TIMES, Oct. 28. 1992, at 24.

410. *Id.*

411. Weston and Corrigan, *supra* note 408.

412. Weston and Corrigan, *Sir Leon Brittan Joins Row Over Capital Standards*, FIN. TIMES, Oct. 29, 1992, at 22.

413. Corrigan, *SEC and Regulators Deadlocked Over Capital Requirements*, FIN. TIMES, Oct. 30, 1992, at 26.

414. 17th *Communique*, *supra* note 367, at 4.

415. *Id.*

ing Party was constituted in 1993. It is presently concentrating on open-end collective investment schemes.

VIII. THE RUSSIAN FEDERATION AND THE CENTRAL ASIAN REPUBLICS[416]

A. *The Russian Federation*

With the collapse of the Soviet Union and the massive transformation from state to private property ownership, the recently formed Russian Republics have begun to enact a body of securities and corporate laws designed to effect and regulate these sweeping changes. While such laws are in the process of formation, they are oftentimes incomplete and suffer shortcomings in both scope and enforcement, the achievement of creating such an extensive corporate and securities rubric within a few short years should not be overlooked. In the largest and most prominent of the Russian Republics, the Russian Federation (or "Russia"), numerous presidential edicts, government decrees and resolutions have been promulgated addressing a broad range of corporate concerns, including the massive privatization and corporatization effort and the regulation of joint-stock companies, investment funds, stock exchanges, foreign investment and shareholders' rights.

While investing in Russia is still a difficult and risky business, the promulgation of such legislation leads the way to the development of a more orderly and workable system, more in keeping with international, western and U.S. business standards. Enactment of corporate and financial legislation is necessary to create and sustain corporate structures in what will hopefully be the continued development of a functioning market economy. Such continued and sustained development will be a factor in giving international companies and enterprises the confidence to make investments and engage in corporate activities in this region in the years to come.

B. *Privatization*

Since reforms began in 1991, it has been reported that 70 percent of state and municipally controlled industry has been privatized and, of these enterprises, two-thirds are profitable.[417] By the end of 1994, it is projected that between 80 and 85 percent of Russia's small enterprises and shops, of which there are reported to be about one million,[418] are to be privately held, the state having already privatized

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416. Prepared by Bonnie H. Weinstein (J.D. 1983, The University of Chicago). Weinstein is a corporate and securities lawyer practicing in New York and Washington, D.C.

417. *Russian Private Sector Dominant*, WALL ST. J., Aug. 10, 1994, at A11.

418. *Id.*

75 percent of its 20,000 medium and large enterprises.[419]

The Russian privatization effort commenced in July 1991 with the enactment of the statute entitled, "RF Privatization of State and Municipal Enterprises Act"[420] which, as stated in its preamble, "sets forth the legal and organizational principles for transforming property relations in producer goods in the Russian Federation through privatization of state and municipal enterprises, with the aim of creating an efficient and socially oriented market economy."[421] Since then numerous additional presidential edicts and legislative enactments have been promulgated to address the regulation of this massive change of property ownership. Of special significance are presidential edicts issued in August 1992 and February 1993 which give effect to the system of privatization vouchers.[422]

Privatization basically occurs as follows. In the instance of the privatization of large concerns (defined as enterprises with assets in excess of 50 million rubles at July 1, 1992, or which employ more than 1,000 workers),[423] a privatization plan, whereby the enterprise will be corporatized into an open joint-stock company, is prepared by the enterprise's management and workers as well as by related state agencies. The plan is then subject to approval by the State Committee for the Management of State Property (the "Goskomimushchestvo" or "GKI"), the agency with primary responsibility for privatization. Under this process, shares representing an equity interest in an enterprise are first given to the enterprise's employees and managers free of charge, and oftentimes to the appropriate employee stock fund, with additional shares offered to these parties at favorable rates. In addition, the local GKI will in many instances retain shares, especially in the case of "strategic industries" such as aerospace and defense enterprises, often maintaining a controlling interest.[424] The remaining shares, which revert to the state property fund, are then permitted to be purchased publicly through voucher auctions and public tenders by other Russian citizens, foreigners, and the numerous Russian-based investment funds which have proliferated since the commencement of

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419. *Investment Push for Russia*, WALL ST. J., May 19, 1994, at A11.

420. IF Privatization of State and Municipal Enterprises Act, RSFSR Supreme Soviet Chairman B. Yeltsin, RSFSR House of Soviets, Moscow (July 3, 1991, with amendments and addenda No. 2930-1, June 5, 1992).

421. *Id.*

422. *See, e.g.*, Edict Enacting RF System of Privatization Vouchers; Statute of Privatization Vouchers, RF Presidential Edict No. 914 (Aug. 14, 1992); Measures to Regulate the Movement and Cancellation of Privatization Vouchers, RF Presidential Edict No. 216 (Feb. 12, 1993); State Guarantees for Right of Citizens of Russia to Participation in Privatization, RF President's Edict No. 640 (May 8, 1993).

423. Similar but different legislation and presidential edicts address the privatization of small and medium-sized businesses.

424. PRIVATIZATION IN EMERGING MARKETS, a co-publication by WORLD EQUITY and the INTERNATIONAL FINANCE CORPORATION (IFR Publishers, 1993), at 44.

privatization. In late 1992, the government issued millions of vouchers, each with a face value of 10,000 rubles, to all Russian citizens. These vouchers, which were originally set to expire on June 30, 1994, allow the holders thereof to purchase shares in the enterprise of their choice or to sell the vouchers to others. Since buying through the voucher auctions often proved problematic for foreign investors due to conflicting laws and tax considerations, these investors have found tenders an attractive alternative to share purchase.[425] Since mid-1993 there have been many successful foreign tenders, whereby a block of shares is tendered by a particular enterprise to a strategic foreign investor.[426] Management is often desirous of foreign partners with complementary business goals as a means ot preventing possible hostile takeover attempts.[427] In May 25, 1994, it was reported that 117 million of the 148 million vouchers that were issued in connection with the privatization process had been collected.[428]

A prospectus is required to be distributed to all investors prior to an equity purchase, and must include financial statements as to the value of the enterprise. However, because the valuation of the enterprise is based on historical book value, which reflects non-market values established under the Soviet command economy, without accounting for inflation, and generally bears no relation to market values, enterprises may be improperly valued which presents attractive opportunities for foreign investment.[429] Since financial data included in the prospectus is largely considered deficient by international accounting standards, a personal knowledge of the business should be acquired and extensive due diligence undertaken prior to investment to determine the true value of the proposed investment.

June 30, 1994 was scheduled to be the deadline for the conclusion of the voucher phase, considered to be the first phase of the privatization process, with cash to be substituted in the post-voucher phase. One of the benefits of using cash is the hope of making foreign investment a less cumbersome process. In addition, in this second phase many of the former Soviet enterprises are to become fully privatized, with the state relinquishing its shares of equity ownership. Recently, it has been determined that there will be continued use of vouchers during a longer transition period. In Moscow, for example, use of the vouchers has been guaranteed through the end of 1994.[430]

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425. *Id.*

426. *Id.* at 45.

427. *See, e.g., id.*, and *Russian Shares: Piercing the Veil*, ECONOMIST, Mar. 12, 1994, at 90.

428. THE CURRENT DIGEST OF THE POST-SOVIET PRESS, NO. 23 at 15 (July 6, 1994).

429. *E.g.*, PRIVATIZATION IN EMERGING MARKETS, *supra* note 424, at 45; *Investment Push for Russia*, WALL ST. J., May 19, 1994, at A11.

430. THE CURRENT DIGEST OF THE POST-SOVIET PRESS, NO. 26 at 5 (July 27,

C. *Joint-Stock Companies*

Under privatization, large enterprises are corporatized into joint-stock companies, which are regulated by statute.[431] Pursuant to this legislation, every such company is required to be registered with the Ministry of Finance. This legislation operates in much the same way as state corporate law statutes do in the United States, and includes requirements relating to organizational structure, shareholders and the board of directors, authorized capital shares, stock certificates, dividends and related matters.

D. *The Stock Markets*

Shares of stock representing equity interests in former state and municipal enterprises can be bought and sold on various stock and commodity exchanges which, while functional, generally operate on a rudimentary level. There are stock and commodity exchanges in operation in Moscow, St. Petersburg, Vladivostock and other major cities.

On the Moscow Central Stock Exchange (the "Moscow Exchange" or "Exchange"), trades in stocks (54.5 percent of total sales in 1993) and bills, a new form of debt security for the Russian market (43.8 percent of total sales in 1993) predominate.[432] In 1993 trades in options represented 0.0001 percent of the Moscow Exchange's activity, which reflects the underdevelopment of the futures and options markets in Russia generally.[433] At July 1993, the Moscow Exchange included the stock of 39 of the country's largest commercial banks (banks, in general, are a popular investment choice for Russians) industrial enterprises and trade companies.[434] Recently, the Exchange adopted stricter listing requirements despite the short-term effect of temporarily forfeiting listings to other exchanges with less stringent requirements.[435] In 1992 transaction volume for the entire year dropped to 74.9 million rubles compared with transaction volume of 271.8 million rubles for the period from August to September 1991.[436] Nonetheless, by February 1994, the Exchange regained its preeminence becoming one of the most highly liquid secondary markets in Russia. In 1993, volume totaled 779.3 rubles, a ten-fold increase from

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1994).

431. Enacting the Statute of Joint-Stock Companies; Statute on Joint Stock Companies, RSFSR Council of Ministers Decree, No. 601 (Dec. 25, 1990, as amended by No. 255, Apr. 15, 1992).

432. *1993 Activities of Moscow Central Stock Exchange, Prospects for 1994*, CENTRAL EURASIA WEEKLY, Feb. 24, 1994, at 52.

433. *Id.*

434. *Id.*

435. *Id.*

436. *Id.*

the previous year.[437]

Despite these successes, the Russian securities markets generally retain the features of small developing markets, in which primary offerings are predominant and the volume and liquidity of the secondary market are low.[438] The basic features of the markets include an underdeveloped material base and infrastructure. In addition, corruption, massive swindles, and fraud have been major problems.[439] In an attempt to stem the pervasive securities scams, such as the recent and much documented MMM investment scandal, fraudulent practices, and irregularities in the securities markets, and institute general standards with respect to the regulation of the industry, on November 10, 1994, President Yeltsin issued an edict entitled "On Measures for State Regulation of Securities Market." At the same time the "statute on the Federal Commission on Securities and the Stock Market under the Russian Federation Government," was enacted.

The laws were enacted after much debate, infighting, and behind the scenes manuevering among those with direct and oftentimes competing interests, viz. the Central Bank, the State Property Committee, the Ministry of Finance, tax regulators, business owners, and an array of related private and government interests. The promulgation of these enactments is seen as a compromise between those in favor of strict government control and the creation of self-regulating mechanisms advocated by business interests.

Most significantly, the edict authorizes the creation of a federal securities commission, with broad powers, including the power to regulate and monitor compliance, issue decrees and directives in such connection, and the ability to regulate and license brokers, dealers, and other industry professionals. The edict requires the licensing and monitoring of banks, insurance companies, and related institutions in their participation in the securities markets and exchanges. The legislation authorizes the creation of a system for ensuring investors' rights and monitoring the compliance of issuing bodies, and creating rules and regulations for the creation of regional securities commissions. Under the edict, information issued with respect to securities are to be regulated by the commission.

Importantly, the edict requires that within three months' time,

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437. *Id.*

438. *Id.* at 52.

439. *See, e.g., Russia Warns of Swindles*, WALL ST. J., May 23, 1994, at 6; *A New Russia: Now Thrive the Swindlers*, N.Y. TIMES, May 6, 1994, at A10. As one top Russian official in the Russian Securities and Exchange Commission reported in response to the recent MMM investment fund scandal, because of a dearth of efficient laws and an abundance of official inertia "the state is incapable" of cleaning up the securities markets. Russian officials generally claim they have little control over their securities markets, and cannot effectively prevent securities scandals. *Id.*

the Commission submit draft legislation with respect to regulating criminal violations of the securities laws. In agreement with the central bank, the Commission also is required to adopt measures to stop entrepeneurial activities undertaken without the appropriate licenses, ban the issuance and circulation of securities not envisioned by and in violation of Russian federal laws, and prohibit the issuance and circulation of securities not registered in the prescribed manner.

The "Statute on the Federal Commission's duties include: the formulation of policy with respect to the development of the securities markets and the coordination of the activities of the relevant state organs regarding the same; ratification of the standards for the preparation and issuance of prospectuses and the registration of securities offerings, including those issued by foreign entities in Russia; formulation of uniform standards with respect to record keeping, and the public circulation of quotations and listing requirements; licensure of professional activity with respect to the securities market; determination of standards with respect to investment and nonstate pension funds; and formulation of recommendations with respect to stock exchange and related market activities.

In addition, the Commission has the authority to establish mandatory in-house capital and other requirements to limit the risks on operations involving professional participants, to refuse to issue licenses or have such licenses suspended or revoked in instances when it determines that stock exchanges or other self-regulating institutions are acting improperly and illegally, carry out spot checks to verify the validity of issuing bodies and professional participants to insure compliance, as well as to conduct audits and checks of issuing bodies.

E. *Investment Fund Regulation*

Investment or mutual funds, which have proliferated in recent years despite frequent scams associated with them, are licensed by the Ministry of Finance. The Statute of Investment Funds[440] addresses the registration requirements of all types of these funds, with the exception of specialized privatization investment funds which accumulate citizens' privatization vouchers and are addressed by separate enactment.[441] An investment fund is deemed to be any publicly held joint-stock company the activities of which include engaging in the attraction of capital through the issuance of its own shares, investment of its own capital in securities of other issues, and trading in securities.[442] The statute requires that the title of the investment fund include the

440. Organization of Securities Market as State and Municipal Enterprises are Privatized, RF President's Edict No. 1186, including annexes Nos. 1 and 3 to 6 (Oct. 7, 1992) [hereinafter Edict No. 1186].

441. *Id.* at Annex No. 2.

442. *Id.* at Annex No. 1.

words "investment fund" and that the fund's founders adopt bylaws written in conformity with Model Bylaws, implement a depositary contract based on a Model Depositary Contract (included as addenda to the statute),[443] elect a board of directors and employ a fund manager, pursuant to specified requirements.[444]

In addition to the statutory requirements which apply to joint-stock companies, the bylaws which govern investment funds must specify whether the fund is open-end or closed-end. In addition, the bylaws must contain an investment declaration stating the main purposes of and any restrictions on the investment activity of the fund, the maximum or minimum amounts of authorized capital which may be invested in various securities, and the procedure for the attraction of loan funds. Further, the bylaws must contain a statement to the effect that all of the investment fund shares shall be ordinary shares with equal voting rights and have the right to receive assets at the fund's wind-up. The bylaws must identify whether the fund has a limited or unlimited period of activity, prohibit the creation of any kind of special or reserve funds, and contain information as to the place, procedure and timing of dividend payments.[445] The authorized capital of the investment fund must be contributed at the fund's inception by its founders and must constitute at least one million rubles, with the first subscription of investment fund shares to be issued within three months of the fund's registration.[446] In order to register share issuances, the fund is required to file with the appropriate financial agencies a prospectus in accordance with the Model Prospectus.[447]

While the above enactments address the registration requirements with respect to investment funds, there are few mechanisms in place to handle the pervasive problems of scandal and fraud occurring in connection with such funds. This continues to be an on-going problem and deterrent to foreign investment.[448]

F. *The Central Asian Republics*

Due to the vast wealth of their natural resources, the five Russian Republics (generally referred to as the Central Asian Republics, viz. Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan) are becoming increasingly significant to the international business community. These republics, in keeping with what has been occurring in the Russian Federation, have been privatizing and corporatizing

443. *Id.* at Annexes Nos. 3 and 4.
444. *Id.*, Annex No. 1.
445. *Id.* at ¶ 9.
446. *Id.* at ¶ 12.
447. *Id.* at Annex No. 6.
448. *Id.*

their state-owned enterprises, and — some at a rate faster than others — are in the process of beginning to enact their own corporate and securities laws to accomplish these aims. Provided below is a brief description of some of the new laws enacted in Kazakhstan and Kyrgyzstan, two of the more developed republics.

G. *Kazakhstan*

With extensive oil, gas and mineral deposits, and a popularly elected president, Kazakhstan is increasingly being viewed as an important potential investment location by the international business community. Philip Morris and Chevron, for example, have recently undertaken projects in the country. Kazakhstan, like the Russian Federation, is in the process of privatizing its formerly stated-owned enterprises, based on a voucher system,[449] and has been enacting legislation (albeit with far fewer and less defined enactments than the Russian Federation[450]), with respect to its new corporate structures, as well as basic legislation addressing foreign investments,[451] banking,[452], taxes[453] and currency.[454]

On February 13, 1991, Kazakhstan set forth the foundation of its corporation law by issuing "The Law on Enterprises."[455] Such legislation, as stated in its preamble, "defines the overall legal, economic, and social principles governing the organization and activities enterprises under market conditions and under various forms of ownership."[456] The law provides for corporate structures to be owned individually, by juridical persons or by the state. Enterprises may be organized as corporations (either for private profit, or for charitable, religious, or other social purposes), partnerships, joint ventures with foreign participation or state enterprises. The statute provides incorporation requirements for such enterprises, including by-law and state registration requirements, and sets forth the activities that require licensure from appropriate state authorities, including conducting geological surveys, exploiting mineral deposits, forest or water reserves, and manufactur-

449. *Law on Denationalization and Privatization of 1991*, from the KAZAKHSTANSKAIA PRAVDA, Aug. 1, 1991, *as published in Russia and the Republics Legal Matters*, THE PARKER SCHOOL OF FOREIGN AND COMPARATIVE LAW, Columbia University, Binder 1, Release 13, Oct. 1993 (Transnational Juris Publications, Inc. 1994) (J. Hazard, V. Pechota, Eds.).

450. At the present time, there is little in the way of securities or stock market activities or enactments with respect to Kazakhstan.

451. Law on Foreign Investment, (effective Jan. 17, 1991, Release 1, Feb. 1992).

452. Law on Banking of April 14, 1993, Release 16, Apr. 1994.

453. Law on the System of Taxation of December 25, 1991, Release 12, Aug. 1993.

454. Law on Currency Regulation of April 14, 1993, Release 16, Apr. 1994.

455. Law on Enterprises of February 13, 1991, Release 13, Oct. 1993.

456. *Id.* at 1.

ing or selling pharmaceutical, toxic or narcotic products.[457] Also included are requirements concerning enterprise profits, worker income, working conditions, environmental concerns, commercial secrets of state-owned enterprises, credit and accounting relations, prices and price-setting (state regulation of prices occurs only in cases established by the Kazakh Supreme Soviet), liquidation and reorganization.[458] In addition, the government guarantees the enforceability of law, equal protection of the rights of all enterprises regardless of the form of ownership, and equal rights of enterprises in their access to material, labor, natural, intellectual and informational resources, credit and foreign investment. The government also guarantees protection from unlawful seizure and prohibits monopolistic practices.[459]

Of particular interest to foreign investors is the "Law on Foreign Investment,"[460] which provides favorable terms and incentives to attract foreign investment. Such investments, which are licensed by the Kazakh Ministry for Foreign Economic Relations, may be made in any sphere of activity with the exception of the manufacture of products with a direct military purpose. Foreign investments enjoy the same privileges as Kazakh-owned enterprises, with the additional benefits of the right of independent decisions on questions of hiring, dismissal, working hours and compensation of employees.[461] A foreign investor is, however, required to provide for the training of personnel from the local population for the purpose of mastery of the technology being introduced.[462] Property brought into the republic as investments, and not intended for sale, is duty free.[463] Foreigners are also permitted to transfer abroad freely their profits made from their Kazakh investments or from the sale of their interest in a Kazakh business. Nationalization of the foreign venture property is not permitted, except in exceptional cases in which event the government undertakes to compensate the foreign investor accordingly.[464]

Foreign investors also are accorded favorable tax treatment. First, there is the operation of free enterprise zones which permit Kazakhs and foreigners to engage in business activities with complete independence, receiving very favorable regulatory, tax, and customs treatment, and without being subject to price regulatory controls or statutory labor requirements.[465] More importantly, many foreign investment

457. *Id.*
458. *Id.*
459. *Id.* at art. 30, 22.
460. Law of Foreign Investment, *supra* note 451.
461. *Id.* at art. 12, 6.
462. *Id.*
463. *Id.* at art. 16.
464. *Id.* at art. 25.
465. Law on Free Economic Zones in the Kazakh Republic (1991), Release 1, Feb. 1992.

activities are completely tax exempt for a five-year period following the first announcement of a profit, and subject to a tax on profits at a 50 percent reduced rate for the five-year period following thereafter.[466]

H. *Kyrgyzstan*

Kyrgyzstan has also enacted laws with respect to privatization,[467] entrepreneurship and foreign economic activities.[468] Its "Law on General Principles of Destatization, Privatization, and Entrepreneurship," addresses privatization which in Kyrgyzstan occurs by either a gratuitous transfer to its citizens or by state sale.[469] In Kyrgyzstan, privatization is effected by establishing special privatization accounts for its citizens, a method slightly different from voucher privatization. In addition, the statute addresses entrepreneurial and business issues, including the types of recognized corporate entities, such as general and limited partnerships, joint-stock companies,[470] production cooperatives,[471] leasing and collective enterprises,[472] and state and other enterprises.[473] In addition, provisions are made for the registration, termination[474] and bankruptcy[475] of such enterprises,[476] guarantees and protection of entrepreneur's rights,[477] and anti-monopolistic activities.[478] Many of these provisions are basic and rudimentary in scope.

Kyrgyzstan's "Law on Foreign Economic Activities," as stated in its preamble, sets forth the general principles of foreign economic activity in the Republic, the procedures for the state regulation of these activities, and the powers of the state authorities in the sphere of foreign economic relations. In this enactment (which is relatively brief), foreign investors are protected against expropriation,[479] free economic zones are referenced[480] and international joint ventures are permitted.[481]

It should be noted that the law in this area is changing rapidly,

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466. Law of Foreign Investment, *supra* note 451, at art. 20.
467. Law on General Principles of Destatization, Privatization, and Entrepreneurship of December 20, 1991, Release 11, June 1993.
468. Law on Foreign Economic Activities of April 18, 1991, Release 6, Oct. 1992.
469. *Id.* at arts. 14 and 15.
470. *Id.* at art. 25.
471. *Id.* at art. 26.
472. *Id.* at art. 27.
473. *Id.* at art. 28.
474. *Id.* at art. 38.
475. *Id.* at Section V.
476. *Id.* at art. 21.
477. *Id.* at art. 32.
478. *Id.* at Section IV.
479. *Id.* at art. 11.
480. *Id.* at arts. 1 and 13.
481. *Id.* at art. 17.

with new enactments constantly being issued and revised. It will be of general interest and great importance to the international legal and business community to see how the securities and corporate laws of the Russian Federation and the Central Asian Republics continue to unfold in the years to come.

IX. CONCLUSION

The principal issues confronting national securities regulators — market volatility, off-exchange trading and market fragmentation generally, the appropriate scope of self-regulation, disclosure, insider trading and other fraud, manipulation, universal banking, capital adequacy, transparency, clearance and settlement, and derivatives — are the same issues that must be dealt with by international securities regulators. A major problem in the international arena, however, is that there are no international law-making institutions vested with the legal authority to address these issues (aside from the European Union which is not open to the international community at large). Accordingly, the question of international securities regulation devolves to a hodge podge of national or non-governmental which are working fitfully, sporadically, and sometimes at cross-purposes on one of the most complex economic problems of our times. Development of a comprehensive system of international securities regulation would serve, at a minimum, two important objectives. First, it would facilitate the process of capital formation pursuant to which capital would be channelled on an intenational basis to its most efficient use, which would enhance the international economic good. Second, the development of a system of international securities regulation could play a major role in averting an international financial crises.[482] Nevertheless, the international community has not, to date, made a major commitment to developing a system of international securities regulation. Only the European Union has developed a comprehensive system of securities regulation that transcends national boundaries.

482. *See* Kaufman, *The Dangerous Volatility in the Financial Markets Isn't Going Away*, WASH. POST, Feb. 4, 1988, at A23, A23.