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SEC Adopts Revisions to the Cross-Border Tender Offer, Exchange Offer and Business Combination Rules and Beneficial Ownership Reporting Rules for Certain Foreign Institutions

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The U.S. Securities and Exchange Commission (the "Commission") has adopted a number of amendments to the rules governing cross-border business combination transactions, which are scheduled to become effective on December 8, 2008.[1] The rules were adopted in substantially the form proposed,[2] with some exceptions, and in large part codify existing staff interpretive and no-action positions and exemptive orders and address recurring areas of conflict or inconsistency between the U.S. rules and foreign regulations and practice.[3]

By adopting the rule amendments, the Commission hopes to encourage bidders for shares of foreign companies to open their offers to U.S. shareholders of those companies. Currently, many bidders exclude U.S. shareholders from offers to avoid the application of the U.S. rules, and they do not take advantage of the Tier I/Tier II exemptions initially adopted in 1999 even when they might be available. While the amendments solve some technical problems with the existing exemptions, in a number of areas they do not go as far as some practitioners had hoped. It remains to be seen whether they will be sufficient to accomplish the Commission's goal of expanding U.S. investor participation in tender offers for foreign issuers.

1 SEC Release Nos. 33-8957; 34-58597 (September 19, 2008) (the "Release").
2 SEC Release Nos. 33-8917; 34-57781 (May 6, 2008) (the "Proposing Release").
3 For these purposes, "cross-border" refers to business combinations in which the target company is a "foreign private issuer," as defined in Rule 3b-4(c) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and rights offerings where the issuer is a foreign private issuer. "Business combination" is defined in Rule 800(a) under the Securities Act of 1933, as amended (the "Securities Act"), as any "statutory amalgamation, merger, arrangement or other reorganization requiring the vote of security holders of one or more of the participating companies. It also includes a statutory short-form merger that does not require a vote of security holders." In the Release, the term is used more broadly to include those kinds of transactions, as well as tender and exchange offers. *See* Securities Act Rule 165(f)(1) (defining the term more broadly to include the types of transactions listed in Rule 145(a), as well as exchange offers).

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The principal changes adopted by the Commission are:

- refining the "look-through" test for calculating U.S. ownership of a target company for purposes of determining eligibility to rely on the cross-border exemptions;
- providing an alternative test to the look-through test based in part on a comparison of average daily trading volume ("ADTV") of the subject securities in the United States and worldwide (for negotiated transactions, the alternative test may only be used if the look-through test is not feasible);
- expanding relief under Tier I for affiliated transactions subject to Exchange Act Rule 13e-3 for transaction structures not covered under the existing cross-border exemptions;
- expanding the relief afforded under Tier II in several ways to eliminate recurring conflicts between U.S. and foreign law and practice;
- codifying existing exemptive orders with respect to the application of Exchange Act Rule 14e-5 for Tier II tender offers;
- expanding the availability of early commencement to offers not subject to Section 13(e) or 14(d) of the Exchange Act, *i.e.*, exchange offers other than for registered equity securities, including by domestic companies for their own debt; and
- permitting specified types of foreign institutions to report on Schedule 13G to the same extent as their U.S. counterparts, without individual no-action relief.

The Commission also reiterates and clarifies the interpretive guidance provided in the Proposing Release regarding the application of certain rules in the area of cross-border business combinations. This interpretive guidance, which became effective on October 9, 2008, includes the Commission's position on:

- the application of the "all-holders" provisions of the tender offer rules to foreign target security holders;
- the ability of non-U.S. bidders to exclude U.S. target security holders in cross-border tender offers; and
- the ability of non-U.S. bidders to use the vendor placement procedure for cross-border exchange offers.

The Commission's full release, including the text of the amendments, is available at http://www.sec.gov/rules/final/2008/33-8957.pdf.[4]

I. Overview of Existing Cross-Border Exemptions

A bid to acquire a non-U.S. company, if made to U.S. holders of that company's securities, may be subject to the U.S. tender offer rules, irrespective of the size of the U.S. holding. In addition, the offer or sale of securities in the United States, whether by way of an exchange offer, in connection with a business combination (such as a merger) or through a rights offering, must be registered under the Securities Act unless an exemption is available. These rules thus differ from the rules of many other countries, the application of which turns not on the residence of the investor, but rather on the jurisdiction of incorporation (or sometimes the jurisdiction of listing) of the target company. This difference reflects one of the fundamental principles of the U.S. securities laws – protection of U.S. investors regardless of the nationality of the bidder or the target and of the investor protections afforded by their regulators in their home markets.

To avoid these U.S. rules, particularly when the percentage of U.S. ownership of the non-U.S. company is relatively small, bidders have often excluded U.S. holders from these transactions. In an effort to discourage this practice, in October 1999, the Commission adopted rules exempting from certain U.S. tender offer regulations and the registration requirements of the Securities Act certain tender and exchange offers involving foreign private issuer[5] targets where the number of U.S. shareholders of the target is limited.[6] In

[4] The Commission's efforts to enhance its rules in the cross-border business combination area are a continuation of recent initiatives to revise the regulatory system applicable to foreign private issuers. *See* SEC Release No. 34-55540 (March 27, 2007), where the Commission adopted amendments to the deregistration rules for foreign private issuers exiting the U.S. regulatory system; SEC Release Nos. 33-8879; 34-57026 (December 21, 2007), where the Commission adopted rules to accept from foreign issuers in their filings with the Commission financial statements prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board; SEC Release Nos. 33-8959; 34-58620 (September 23, 2008), where the Commission adopted rule amendments applicable to foreign issuers to enhance the information available to investors; and SEC Release No. 34-58465 (September 5, 2008), where the Commission adopted amendments to the rule that exempts a foreign private issuer from having to register a class of equity securities under Section 12(g) of the Exchange Act. These rules are discussed in separate memoranda prepared by the firm.

[5] Rule 3b-4 under the Exchange Act defines "foreign private issuer" as a national of any foreign country or a corporation or other entity organized under the laws of any foreign country, unless (1) more than 50% of the issuer's securities are held directly or indirectly by U.S. residents and (2) a majority of the issuer's executive officers or directors are U.S. residents, more than 50% of the issuer's assets are located in the United States or the issuer's business is administered principally in the United States.

[6] *See* SEC Release Nos. 33-7759; 34-42054 (October 22, 1999) (the "Cross-Border Adopting Release"). Although the target (or issuer in a rights offering) must be a foreign private issuer, the acquiror relying on the cross-border exemptions need not be a foreign private issuer and, in fact, may be a U.S. company.

particular, the Commission's rules (i) exempt from most U.S. tender offer rules a qualifying cross-border transaction where U.S. ownership of the securities of the target foreign private issuer is 10% or less ("Tier I exemption");[7] (ii) provide limited relief from certain U.S. tender offer rules if U.S. ownership of the target securities is greater than 10% but 40% or less ("Tier II exemption");[8] and (iii) exempt from Securities Act registration the securities issued in business combination transactions and rights offerings if U.S. ownership of the target is 10% or less.[9] In addition to these U.S. ownership thresholds, the cross-border exemptions are conditioned on other requirements, such as the principle that U.S. target security holders be permitted to participate in the offer on terms at least as favorable as those afforded other target holders.[10] The Commission retained this basic two-tier structure and threshold U.S. ownership percentages in adopting the amendments discussed below.

The Commission's exemptions have met with limited success since they were adopted in 1999. While many acquirors take advantage of the Tier II exemption, relatively few bidders use the Tier I exemption, in part because of technical problems with the rules, and also because they find that the effort and expense of determining whether they qualify for Tier I, and the risk of submitting to U.S. court jurisdiction, are not worthwhile given the small number of additional shares to which they gain access by using the exemption. While the Commission's amendments would appear to improve the rules from a technical perspective, they may not be sufficient to address the more fundamental problem that results from the limited economic incentive bidders have to use the Tier I exemption.

II. Summary of Rule Amendments

A. Modified "Look-Through" Test

The principal change adopted by the Commission relates to the "look-through" test for cross-border exemptions. In order to determine eligibility to rely on any cross-border exemptions, an acquiror must calculate the applicable percentage of the relevant shares held by U.S. holders and, in doing so, must look through the securities held of record by nominees in specified jurisdictions to identify those held for the accounts of persons located in the United States.

For negotiated transactions, acquirors must generally continue to conduct the look-through analysis. However, if acquirors are unable to conduct this analysis, the Commission now provides an alternate test that incorporates elements from the current "hostile

[7] Exchange Act Rule 14d-1(c).
[8] Exchange Act Rule 14d-1(d).
[9] Securities Act Rules 801 and 802.
[10] Securities Act Rules 801(a)(3) and 802(a)(2); Exchange Act Rules 13e-4(h)(8)(ii) and (i)(2)(ii); and 14d-1(c)(2) and (d)(2)(ii).

presumption" for non-negotiated transactions, including an element based on ADTV of the subject securities. The limited circumstances under which this "alternate test" will be available to acquirors for negotiated transactions are discussed below. In contrast, the alternate test is available to all acquirors in non-negotiated transactions.

To address continuing concerns raised by commenters about the look-through test for negotiated transactions, the Commission has revised the manner in which that analysis must be performed.

1. Timing of the Calculation

Under the current rules, the relevant date for determining U.S. ownership for purposes of the look-through analysis is limited to the 30th day before commencement of the transaction for which exemption is being sought. With the adoption of the amendments, acquirors will be permitted to make the U.S. beneficial ownership calculation as of any date that is *no more than 60 days before* and *no more than 30 days after* the public *announcement*[11] of the transaction.[12] The amended rules also specify that where the acquiror is unable to complete the look-through analysis as of this 90-day period, it may use a date within 120 days before public announcement. The Commission had initially proposed allowing acquirors to make the U.S. beneficial ownership calculation on a date chosen by the bidder within a 60-day period before the public announcement of the transaction.

The two key changes – focusing on a range of dates rather than a specific date and keying to announcement rather than commencement – reflect the difficulties transaction participants have had obtaining information as of a specific date, especially in light of the uncertainty of when commencement would actually occur, and address the uncertainty facing acquirors at the time of announcement as to the continued availability of needed exemptions at the time of commencement. Moreover, by permitting a range of dates both before and after public announcement, the rule provides acquirors whose home country law permits them to wait to conduct the analysis until after public announcement to avoid compromising the confidentiality of the proposed transaction to the greatest extent possible.

Keying the look-through analysis to announcement, rather than commencement, also serves to harmonize Tier I and Tier II exemptions with relief under Exchange Act Rule 14e-5, which generally prohibits purchases of target securities outside a tender offer from the

[11] The Commission considers "public announcement" to be any oral or written communication by the acquiror or any party acting on its behalf, which is reasonably designed to inform or has the effect of informing the public or security holders in general about the transaction. *See* generally, Instruction 5 to Exchange Act Rules 13e-4(c) and 14d-2.

[12] *See* amended Securities Act Rule 800(h), Instruction 1.i. to amended Exchange Act Rules 13e-4(h)(8) and (i) and Instruction 2.i. to amended Exchange Act Rules 14d-1(c) and (d).

date of announcement of that offer through its expiration. Tender offers conducted in reliance on the Tier I exemption are exempt from the application of Rule 14e-5 (and by codifying, as part of these rule amendments, the class-wide exemptive relief previously granted, the Commission has extended this exemption in certain areas for Tier II-eligible tender offers).

The Commission's determination to adopt a longer and more flexible "look-through" period for calculating U.S. ownership is based on the staff's experience over the past eight years and its acknowledgement that in some countries it takes longer than 30 days (or even 60 days, as was initially proposed) to perform the analysis or it is not possible to calculate ownership as of a specific date in the past.[13] Furthermore, the Commission recognized that even the new 90-day range may not be enough time in some foreign jurisdictions, permitting acquirors to use a date within a 120-day period before public announcement if circumstances warrant. The Commission did not provide any guidance on the circumstances that would justify relying on the extended period.

In the Proposing Release, the Commission noted that it remains concerned about the possibility that a date for calculation would intentionally be chosen to present a less than representative picture of the target security holder base. The instructions to the cross-border exemptions make it clear that the exemptions are not available for any transaction or series of transactions that technically comply with the Commission's rules but are, in fact, part of a plan or scheme to evade them in practice.

2. Exclusion of Large Target Security Holders

In an effort to increase the number of cross-border business combinations eligible for the exemptions, the Commission adopted amendments that will no longer require that individual holders of more than 10% of the subject securities be excluded from the calculation of U.S. ownership. However, the Commission retained the requirement in the existing rules that securities held by the acquiror be excluded from both the numerator and the denominator in calculating U.S. beneficial ownership.[14] The Commission declined to adopt a more narrow exclusion for securities held by greater than 10% holders that are otherwise affiliated with the target, as recommended by several commenters, because it may be too cumbersome to require acquirors to determine affiliation.

[13] *See, e.g.*, Serono S.A. (September 12, 2002) (cited in footnote 65 of the Proposing Release) (hereinafter "Serono"); Alcan, Inc. (October 7, 2003) (hereinafter "Alcan") (cited in footnote 69 of the Proposing Release); and Equant N.V. (April 18, 2005) (cited in footnote 69 of the Proposing Release).

[14] *See* amended Securities Act Rule 800(h)(2) and Instruction 2.ii. to amended Exchange Act Rules 14d-1(c) and (d). The Commission notes that in assessing what securities should be considered for the U.S. ownership calculation, it is appropriate to exclude those held by the acquiror because the acquiror will not be participating in the acquisition as a target holder.

3. Inability to Conduct Look-Through Analysis

If an acquiror in a negotiated transaction is "unable to conduct" the modified look-through analysis described above, the amendments offer an alternative eligibility test based in part on a comparison of the ADTV of the subject securities in the United States to the worldwide ADTV.[15]

The Commission did not define what is meant by the phrase "unable to conduct," indicating that inability would need to be assessed based on the facts and circumstances of the particular transaction. The Commission notes that the need to dedicate time and resources to the look-through analysis alone will not support a finding that a bidder is unable to conduct the analysis. Similarly, concerns about the completeness and accuracy of the information obtained from the analysis will not necessarily justify the use of the alternate test. In each instance, the bidder must make a good faith effort to conduct a reasonable inquiry into ascertaining the level of U.S. beneficial ownership. For example, if beneficial ownership reports are generated only at fixed intervals during the year and the published information is as of a date outside the range specified in the revised rules or a substantial portion of the subject securities is in bearer form, these facts may be sufficient for the acquiror to conclude that it is unable to conduct a look-through analysis. In addition, in certain foreign jurisdictions, nominees may be prohibited by law from disclosing information about the beneficial owners on whose behalf they hold. Where nominees are prohibited by law from disclosing the country of residence of the beneficial owners of the subject securities, the Commission notes that the alternate test for determining eligibility should be available.

In the non-negotiated context (*i.e.*, where there is no agreement between the target and the acquiror), the Commission recognized, when it adopted the existing cross-border exemptions in 1999, that the look-through analysis would be even more difficult or impossible for third-party acquirors in these transactions, because they would not have the cooperation of the issuer. In particular, obtaining information from nominees that hold for the account of others is difficult for third-party acquirors and may have the effect of alerting the market to a contemplated offer before the acquiror wishes to make its intentions known. For that reason, the Commission included in the original cross-border exemptions a "hostile presumption" that would allow a third-party bidder in a non-negotiated tender or exchange offer to assume that U.S. ownership in the target company is no more than 10% or 40%, the thresholds for Tier I and Tier II, respectively, so long as ADTV in the United States does not exceed 10% or 40%, as the case may be, of the ADTV worldwide over a 12-month period ending 30 days before commencement, and the bidder has no "reason to know" that actual U.S. ownership is inconsistent with that figure (either based on the issuer's informational

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[15] *See* new Securities Act Rule 800(h)(7), Instruction 3 to amended Exchange Act Rules 13e-4(h) and (i) and Instruction 3 to amended Exchange Act Rules 14d-1(c) and (d).

filings with the Commission or foreign regulators or based on the bidder's actual or imputed knowledge from other sources).

The alternate test is similar to and replaces the existing "hostile presumption" and is available for all non-negotiated transactions. The alternate test has three prongs, which are further discussed below.

B. Elements of the Alternate Test

1. ADTV Test

The first prong of the alternate test is satisfied if the ADTV for the subject securities in the United States over a 12-month period ending no more than 60 days before the announcement of the transaction is not more than 10% (or 40% for Tier II) of ADTV on a worldwide basis.[16] The requirement to perform the comparison as of a 12-month period minimizes the potential for manipulation of the trading volumes both inside and outside the United States. Noting that in the context of an objective measure, such as ADTV, there should be no concerns about compromising confidentiality by performing this calculation before announcement, the Commission chose not to permit the acquiror to use a range of dates that extends beyond announcement (as is permitted under the modified look-through test discussed above).

In the case of negotiated transactions, the revised rules also require that there be a "primary trading market" for the subject securities in order for the acquiror to rely on the alternate test.[17] "Primary trading market" means that at least 55% of the trading volume in the subject securities takes place in a single, or no more than two, foreign jurisdictions during a 12-month period ending no more than 60 days before the announcement of the transaction.[18] In addition, if the trading of the subject securities occurs in two foreign markets, the trading in at least one of the two must be larger than the trading in the United States for that class of securities.[19]

The existence of a primary trading market is important in the Commission's view because it ensures that there is a primary foreign regulator with oversight over the

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[16] *See* new Securities Act Rule 800(h)(7)(i), Instruction 3.i. to amended Exchange Act Rules 13e-4(h)(8) and (i) and Instruction 3.i. to amended Exchange Act Rules 14d-1(c) and (d).

[17] Although not proposed, the Commission had solicited comment on whether a primary trading market requirement should be adopted when using an ADTV measure. *See* Section II.A.4 of the Proposing Release.

[18] *See* Exchange Act Rule 12h-6(f)(5)(i).

[19] *See* Exchange Act Rule 12h-6(f)(5)(ii).

transaction. Thus, where there is no primary trading market for the subject securities outside the United States, an acquiror in a negotiated transaction may not rely on the alternate test.[20]

2. Information Filed by the Issuer

The second prong of the alternate test requires the acquiror to consider information about U.S. ownership levels that appears in annual reports or other annual information filed by the issuer with the Commission or with the regulator in its home jurisdiction. The acquiror may be disqualified from relying on the cross-border exemption sought if those reports or other filings indicate levels of U.S. ownership that exceed applicable limits for that exemption.[21]

This element of the alternate test is virtually identical to the comparable element of the existing test for non-negotiated transactions. The only change is that the revised instruction specifies that only annual reports or other annual information filed *before* the public announcement of the transaction must be taken into account by the acquiror. In other words, while an acquiror will not lose eligibility based on reports filed after announcement that indicate a higher U.S. ownership level than what is permitted, neither will it gain eligibility to rely on the exemptions based on reports filed after announcement indicating a reduction in the U.S. ownership level.

3. Reason to Know

The final prong in the alternate test is the "reason to know" element, which is similar to the comparable element in the existing hostile presumption test. This prong of the alternate test provides that an applicable cross-border exemption is not available, even where all other elements of the alternate test are met, if the acquiror "knows or has reason to know" that the U.S. beneficial ownership level exceeds the limit for the applicable exemption.

An acquiror is deemed to have reason to know information about U.S. ownership of the subject class that appears in any filing with the Commission or any regulatory authority in the issuer's home country or (if different) the jurisdiction in which its primary trading market is located.[22] This requirement captures not only filings by the issuer, but also filings by other parties reporting beneficial ownership of the subject securities. For example, acquirors would be presumed to know information about beneficial ownership reflected in filings by third parties with the Commission, such as beneficial ownership reports on

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[20] The primary trading market requirement does not apply to the use of the alternate test in non-negotiated transactions.

[21] *See* amended Securities Act Rule 800(h)(7)(ii), Instruction 3.ii. to amended Exchange Act Rules 13e-4(h)(8) and (i) and Instruction 3.ii. to amended Exchange Act Rules 14d-1(c) and (d).

[22] *See* amended Securities Act Rule 800(h)(7)(iii) and Instruction 3.iii. to amended Exchange Act Rules 14d-1(c) and (d).

Schedule 13D, 13F or 13G, or similar reports filed by third parties in the target's home country and in the country of its primary trading market, if different. The inclusion of Schedule 13F in this list may prove problematic as Schedule 13F is filed by hundreds of institutional money managers without any easy mechanism for searching by company name. Acquirors might consider using outside service companies that regularly compile information from Schedule 13F filings.

The amended rule also contains additional references to specific sources of information that will be attributed to the acquiror.[23] These sources include information about U.S. ownership "available from the issuer or obtained or readily available from any other source that is reasonably reliable." "Readily available" for these purposes means publicly available from sources reasonably accessible to the issuer or acquiror at no or limited cost. Other sources of information about which the acquiror will be deemed to have knowledge under the amended rules include, but are not limited to, third-party information providers and other advisors engaged by the parties to the transaction that may have provided information about U.S. ownership. As in the case of the previous prong, an acquiror is required to take into account only that information it has reason to know *before* public announcement of the transaction. Knowledge or reason to know acquired after public announcement will not disqualify the acquiror from relying on the cross-border exemptions.

C. Changes to Eligibility Test for Rights Offerings

In response to feedback from commenters that many foreign private issuers continue to exclude U.S. holders from rights offerings available to all other security holders, the Commission adopted changes similar to those for business combinations to the method of calculating U.S. ownership for purposes of the exemption for rights offerings. Issuers may now calculate U.S. ownership as of a date *no more than 60 days before and 30 days after the record date* for the rights offering.[24] Thus, issuers will have greater flexibility on the timing of the calculation of U.S. ownership within a range of dates; however, the reference point for the calculation will continue to be the record date for rights offerings, rather than the date of public announcement as in the case of business combinations. Furthermore, the expanded date range of up to 120 days if the information is not available within the range otherwise specified is not available for rights offerings as the issuer has the ability to set an appropriate record date.

[23] *See* amended Securities Act Rule 800(h)(7)(iii), Instruction 3.iii. to amended Exchange Act Rules 13e-4(h)(8) and (i) and Instruction 3.iii. to amended Exchange Act Rules 14d-1(c) and (d).
[24] *See* amended Securities Act Rule 800(h).

The alternate test for calculating U.S. ownership also will be available for foreign private issuers unable to conduct the look-through analysis in a rights offering.[25]

While the final rules relating to the eligibility test reflect improvements over the rules proposed by the Commission in the Proposing Release, they do not go as far as some commenters had suggested to eliminate the "look-through" analysis altogether in favor of an ADTV test for negotiated transactions. It remains to be seen whether the alternate test based on ADTV will be valuable for bidders in negotiated deals, which will depend in part on how comfortable practitioners will be to advise their clients that the inability standard has been met.

D. Changes to the Tier I Exemption: Rule 13e-3

Rule 13e-3 under the Exchange Act establishes specific filing and disclosure requirements for certain affiliated transactions[26] with the purpose or effect of "going private"[27] because of the conflicts of interest inherent in such situations. Cross-border transactions where the U.S. ownership is 10% or less conducted by the issuer or its affiliates under the existing Tier I exemption and Securities Act Rule 802 are currently exempt from the requirements of Rule 13e-3. However, the scope of the existing Tier I exemption from Rule 13e-3 does not apply to some business combination transaction structures commonly used abroad. These include schemes of arrangement, cash mergers, compulsory acquisitions for cash and other types of business combination transactions.

The Commission acknowledges that the heightened disclosure requirements of Rule 13e-3 represent a significant disincentive for acquirors to include U.S. security holders in cross-border transactions that do not currently fit within the Rule 13e-3(g)(6) exemption, particularly where U.S. holders make up no more than 10% of the target shareholder base. Recognizing that the form of the transaction structure should not prevent an otherwise-

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[25] *See* new Securities Act Rules 800(h)(6) and (7). This is a change from the existing rules where the hostile presumption based in part on the ADTV comparison is available only for third-party, unaffiliated acquirors. *See, e.g.*, existing Securities Act Rule 802(c), which applies only to persons other than the issuer of the subject securities and is being replaced by the alternate test.

[26] The kinds of transactions covered by Exchange Act Rule 13e-3 include tender offers, purchases of securities, mergers, reorganizations, reclassifications and sales of substantially all the assets of a company. *See* Rule 13e-3(a)(3)(i)(A) - (C).

[27] Exchange Act Rule 13e-3(a)(3)(ii) lists the effects that will cause the rule to apply to a specified transaction: (A) causing any class of equity securities of an issuer which is subject to Section 12(g) or Section 15(d) of the Exchange Act to be held of record by fewer than 300 persons; or (B) causing any class of equity securities of the issuer which is listed on an exchange or quoted on an interdealer quotation system to no longer be so listed or quoted. For foreign private issuers engaged in transactions that would have a going private effect under the rules, the Commission interprets Rule 13e-3 to apply where the transaction results in fewer than 300 security holders of record in the United States. *See* SEC Release Nos. 33-8959; 34-58620 (September 23, 2008).

eligible issuer or affiliate from relying on the Tier I exemption from Rule 13e-3, the Commission eliminated all limits on the kinds of cross-border transactions that could be covered under the exemption in Rule 13e-3(g)(6). In order to qualify for the expanded exemption from Rule 13e-3, a party must meet all of the conditions for reliance on Rule 802 or Tier I.

E. Changes to the Tier II Exemption

Unlike the Tier I exemption and the Securities Act Rule 801 and 802 exemptions, the Tier II exemption does not exempt third-party bidders or issuers from applicable U.S. filing, disclosure, dissemination and procedural requirements for tender offers or going-private transactions subject to Rule 13e-3. Transactions eligible for the Tier II exemption also do not have corresponding relief from the registration requirements of Section 5 of the Securities Act.

1. Clarify that Tier II Relief Applies Where Target Securities Are Not Subject to Rule 13e-4 or Regulation 14D

Under existing rules, there is some uncertainty whether the Tier II exemption applies only to transactions governed by Regulation 14D and Rule 13e-4 under the Exchange Act,[28] or also is available when a tender offer is governed by Regulation 14E only.[29] Tender offers governed by Regulation 14E only include, for example, offers for unregistered equity and cross-border debt tender offers. The Commission amended its rules as proposed to address this uncertainty. Bidders that otherwise meet the conditions for reliance on the Tier II cross-border exemption may now rely on that relief in making such tender offers, to the extent applicable, regardless of whether the target securities are subject to Rule 13e-4 or Regulation 14D.[30]

Certain of the relief afforded under the Tier II exemption will not be necessary in the case of offers not subject to Rule 13e-4 or Regulation 14D. For example, because the "all-

[28] Regulation 14D and Rule 13e-4 apply only to tender offers for equity securities. Regulation 14D applies only where the equity security that is the subject of the tender offer is registered under Section 12 of the Exchange Act, and where the bidder makes a partial offer for less than all of the outstanding securities of the subject class and could own more than 5% of those securities when purchases in the tender offer are aggregated with its existing ownership of those securities. Rule 13e-4 applies to an issuer equity tender offer where the subject securities are not themselves registered under Section 12, but where the issuer has another class of securities that is so registered.

[29] Regulation 14E applies to all tender and exchange offers, whether for debt or equity, and whether or not the security is registered under Section 12. The Commission also adopted a technical amendment to the definition of Regulation 14E in Rule 14d-1(a) to clarify that it encompasses the entire regulation, including Rules 14e-1 through 14e-8. The current definition includes only Rules 14e-1 and 14e-2 and was not amended when the additional rules were adopted under Regulation 14E.

[30] *See* amended Exchange Act Rules 13e-4(i) and 14d-1(d).

holders" requirement[31] does not apply to such offers, the Tier II provision permitting the use of a dual offer structure may be unnecessary. Under the revised rules, the Tier II exemptions will be available to Regulation 14E-only offers where the exemptions would have been available if those offers were subject to Rule 13e-4 or Regulation 14D. This is consistent with this firm's long-held view that the Commission intended Tier I and Tier II to be available whether or not Rule 13e-4 or Regulation 14D applies.

2. Expand Tier II Relief for Dual or Multiple Offers

The Commission also clarified the relief afforded under Tier II in the following ways to help eliminate recurring conflicts between U.S. and foreign law and practice:

- permit the offeror to make more than one non-U.S. offer;
- allow the U.S. offer to include non-U.S. persons and the foreign offer(s) to include U.S. persons; and
- clarify that bidders relying on the dual offer provision in the Tier II exemption to conduct separate U.S. and non-U.S. offers for less than all of a class of target securities must use a single proration "pool."

U.S. tender offer rules require that when a bidder makes a tender offer subject to Rule 13e-4 or Regulation 14D under the Exchange Act, that tender offer must be open to all target security holders of the subject class. The Tier II cross-border exemption currently contains a provision permitting a bidder conducting a tender offer to separate that offer into two separate offers – one U.S. and one foreign – for the same class of securities. By permitting the use of two separate but concurrent offers – one made in compliance with U.S. rules and the other conducted in accordance with foreign law or practice – the dual offer provision facilitates cross-border tender offers.

In practice, however, issues have arisen because the text of the exemption specifically permits only *two* offers for the target class of securities. Bidders may be required to (or may wish to) make more than one offer outside the United States. This may be the case, for example, where the primary trading market for the target's securities differs from the target's country of incorporation. Noting that it has, upon request, granted relief permitting multiple foreign offers,[32] the Commission eliminated the restriction on the

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[31] *See* Exchange Act Rules 13e-4(f)(8) and 14d-10(a).

[32] *See, e.g.*, Mittal Steel Company N.V. (June 22, 2006) (cited in footnote 150 of the Release).

number of non-U.S. offers a bidder may make in a cross-border tender offer by changing the references to "dual offers" to "multiple offers."[33]

In addition, the Commission revised the multiple offer provisions to allow a U.S. offer to be made to U.S. holders of the subject securities and *all* holders of American Depositary Receipts ("ADRs") representing interests in the subject securities, including foreign holders. This revision codifies relief afforded in numerous cross-border transactions under the existing rules, because bidders generally prefer to include all holders of ADRs in a single offer.[34] The U.S. offer must be made on terms at least as favorable as those offered any other holder of the subject securities. The rules are not intended to enable an offer to be made only to holders of ADRs or only to holders of the underlying securities, where the target shares are registered under Section 12 or where Rule 13e-4 otherwise applies. The Commission notes that it views ADRs and the underlying securities as a single class for purposes of the tender offer and beneficial ownership reporting rules. The rules have not been revised to allow foreign target holders who do not hold in ADR form (*i.e.*, who hold in direct share form) to participate in U.S. offers.

The changes to Exchange Act Rules 13e-4(i)(2)(ii) and 14d-1(d)(2)(ii) also permit U.S. persons to be included in the foreign offer(s) where the laws of the jurisdiction governing such foreign offer(s) expressly preclude the exclusion of U.S. persons from the foreign offer(s) and where the offer materials distributed to U.S. persons fully and adequately disclose the risks of participating in the foreign offer(s). The Commission also clarifies that bidders relying on the dual offer provision in the Tier II exemption to conduct separate U.S. and non-U.S. offers for less than all of a class of target securities must use a single proration "pool," in accordance with the existing requirements of the rules.[35] This is to assure equal treatment of security holders who have tendered their securities.

3. Termination of Withdrawal Rights While Tendered Securities Are Counted

The Commission adopted as proposed rule revisions to address certain issues relating to the "back-end" withdrawal rights required under Section 14(d)(5) of the Exchange Act and Rule 13e-4(f)(2)(ii) under the Exchange Act for tender offers conducted under the Tier II cross-border exemption. New provisions have been added to the Tier II exemption to permit the suspension of back-end withdrawal rights during the time after the initial offering period when tendered securities are being counted and before they are accepted for

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[33] *See* amended Exchange Act Rules 13e-4(i)(2)(ii) and 14d-1(d)(2)(ii).

[34] *See, e.g.*, Serono, Alcan and Southern Cross Latin America Private Equity Fund, L.P. (March 5, 2002) (cited in footnote 158 of the Release).

[35] *See* Section 14(d)(6) of the Exchange Act and Rules 13e-4(f)(3) and 14d-8.

payment.[36] Both of the back-end withdrawal rights provisions require bidders to provide withdrawal rights after a set date (60 days), measured from the commencement of a tender offer.[37] Thus, even where a tender offer has technically closed and tenders are no longer being accepted, back-end withdrawal rights may exist until the offeror accepts tendered shares for payment.

The Commission points out that differences in the tender, acceptance and payment procedures between U.S. and foreign offers necessitate this relief. Unlike in the United States, where employment of a single exchange agent permits bidders to know at any point in the offering period the number of securities tendered, the mechanics of the tender process in non-U.S. tenders, including centralizing and counting tendered securities, may take an extended period of time. The bidder in a cross-border tender offer may not know whether the minimum tender condition has been satisfied immediately after the end of the initial offering period. The bidder cannot accept tendered securities until all offer conditions, including the minimum tender condition, have been satisfied or waived and the counting process is completed.

The revised rules codify relief from back-end withdrawal rights that the Commission has previously granted in connection with cross-border transactions.[38] Both third-party bidders for securities of a foreign private issuer and foreign private issuers repurchasing their own securities would, subject to the conditions outlined in the rules, be able to suspend back-end withdrawal rights while tendered securities are being counted, even where no subsequent offering period is provided.[39] The rules are conditioned on the following factors:

- the Tier II exemption must be available;
- the offer must include an offering period, including withdrawal rights, of at least 20 U.S. business days;
- at the time withdrawal rights are suspended, all offer conditions must have been satisfied or waived,[40] except to the extent that tendered securities are being counted to determine if the minimum acceptance condition has been satisfied; and

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36 *See* new Exchange Act Rules 13e-4(f)(2)(v) and 14d-1(d)(2)(viii).

37 *See* Section 14(d)(5) of the Exchange Act.

38 *See, e.g.*, Serono.

39 The amended rules also operate to suspend withdrawal rights that may exist after the expiration of a subsequent offering period, to the extent the bidder meets the conditions outlined in the rules.

40 The Commission takes the view that the only conditions that may survive the expiration of an initial offering period are regulatory approvals necessary to consummate the tender offer.

- withdrawal rights are suspended only during the necessary centralization and counting process period and are reinstated immediately thereafter, except to the extent they are terminated by the acceptance of tendered securities.

4. Expanded Relief for Subsequent Offering Periods

Current rules permit a third-party bidder in a tender offer for all of the subject class of securities to include a subsequent offering period during which securities may be tendered and purchased on a rolling or "as tendered" basis if certain conditions are met.[41] The revised rules eliminate the current 20 U.S. business day limit on the length of the subsequent offering period. As proposed, this rule change would have applied only to Tier II cross-border tender offers. However, recognizing that the flexibility to conduct a longer subsequent offering period will be beneficial to bidders and target security holders in U.S. offers as well, the Commission made this change to its tender offer rules generally.[42]

The elimination of the 20 business day time limit will allow security holders more time to tender during the subsequent offering period. Tendering holders will be paid more quickly, thereby avoiding the lengthy process that may be associated with a "squeeze-out" merger. The Commission notes that security holders tendering during a subsequent offering period will continue to be protected by the prompt payment provisions, as modified in the case of Tier II offers (as discussed below), in the event that a subsequent offering is conducted over an extended period of time.

The Commission also addressed the requirement under the U.S. rules that bidders must immediately accept and promptly pay[43] for all securities "as they are tendered during the subsequent offering period."[44] This requirement may conflict with market practice in non-U.S. jurisdictions. The Commission is amending the rules to allow a bidder in a cross-border tender offer conducted pursuant to the Tier II exemptions to "bundle" and pay for securities tendered in the subsequent offering period within 20 business days[45] of the date of tender (in contrast to the current rule requiring daily aggregation of securities tendered during the subsequent offering period).[46] Because the maximum time period for the subsequent offering period is being eliminated under the amended rules, the Commission chose not to adopt the recommendation of certain commenters to allow bidders to pay for tendered securities in accordance with the target's home country law or practice. The

41 *See* Exchange Act Rule 14d-11.
42 *See* amended Exchange Act Rule 14d-11.
43 Prompt payment is generally understood to mean within three business days.
44 *See* Exchange Act Rule 14d-11(e).
45 For purposes of this rule provision only, a business day will be determined by reference to the relevant foreign jurisdiction. *See* Exchange Act Rule 14d-1(d)(2)(iv).
46 The Commission had initially proposed to require payment within 14 business days.

Commission notes that without a time limit for payment, investors tendering securities in the subsequent offering period may face an indefinite waiting period for payment of their tendered securities. Maintaining a time limit is particularly important because target security holders who tender during the subsequent offering period do not have withdrawal rights.[47] Where local law mandates and local practice permits payment on a more expedited basis, payment must be made more quickly than 20 business days from the date of tender to satisfy U.S. prompt payment requirements.

The Commission did not adopt corresponding changes to prompt payment practice during the subsequent offering period for domestic offers, noting that the changes in prompt payment practice for Tier II cross-border tender offers are necessitated by direct conflicts between U.S. and foreign law and practice, and no such conflicts exist for U.S. offers.

Another area of conflict involving subsequent offering periods relates to the requirement, in certain foreign jurisdictions, that bidders pay interest on securities tendered during the subsequent offering period. Paying interest on securities tendered during a subsequent offering period conflicts with the equal treatment principles in Rule 14d-10(a)(2). The Commission adopted, as proposed, a rule change permitting a departure from Rule 14d-10(a)(2) for the payment of interest for securities tendered during a subsequent offering period in a Tier II cross-border tender offer where required under foreign law.[48] The Commission's rule change does not permit the payment of interest on securities tendered during the initial offering period.

The final issue with respect to subsequent offering periods addressed by the Commission relates to cross-border tender offer structures that include a "mix and match" election feature. In mix and match offers, target security holders are offered a set mix of cash and securities of the bidder – often referred to as the "standard entitlement" – with the option to elect a different proportion of cash and securities to the extent that other tendering security holders make opposite elections. The bidder typically sets a maximum amount of cash or securities that it will issue in the offer. To the extent that more tendering target security holders elect cash or bidder securities, their elections are prorated to the extent they cannot be satisfied through "offsetting elections" made by other target security holders.

Mix and match offers often conflict with U.S. requirements applicable to the subsequent offering period.[49] Those rules provide that a bidder may offer a choice of different forms of consideration in the subsequent offering period, but only if there is no

[47] *See* note to Exchange Act Rule 14d-11.

[48] *See* new Exchange Act Rule 14d-1(d)(2)(vi).

[49] The Commission did not extend its changes to accommodate mix and match offers to tender offers for U.S. issuers since, in the United States, a mix and match offer often can be achieved through a statutory merger.

ceiling on any form of consideration offered. In addition, the rules require a bidder to offer the same form and amount of consideration to tendering security holders in both the initial and subsequent offering periods. In these kinds of offers, bidders want to impose a maximum limit on either (or both) the number of securities or the amount of cash they will be obligated to deliver if the offer is successful. In addition, the offset feature characteristic of mix and match offers is inconsistent with the prohibition on offering different forms and amounts of consideration in the initial and subsequent offering periods.

The Commission adopted, as proposed, revisions to its rules specifically to allow separate offset and proration pools for securities tendered during the initial and the subsequent offering periods in an offer conducted under Tier II.[50] The Commission notes that these changes are necessary and appropriate to facilitate the prompt payment for securities tendered during these offer periods, and to permit the use of the mix and match offer structure generally. Citing the same practical considerations, the Commission also eliminated the prohibition on a "ceiling" for the form of consideration offered in the subsequent offering period in an offer conducted under Tier II, where target security holders are given the ability to elect between two or more different forms of offer consideration.[51]

5. Additional Guidance Regarding Termination of Withdrawal Rights After Reduction or Waiver of a Minimum Acceptance Condition

The U.S. tender offer rules generally provide that a bidder must allow an offer to remain open for a certain period of time after a material change in its terms is communicated to target security holders and that the bidder must provide withdrawal rights during such period. In the Cross-Border Adopting Release, the Commission affirmed the staff's then interpretive position that a bidder meeting the conditions of the Tier II exemption may waive or reduce the minimum acceptance condition without providing withdrawal rights during the time remaining in the tender offer after the waiver or reduction, subject to certain specified conditions.[52]

The Commission affirmed, with some modifications, its guidance in the Proposing Release limiting the interpretive position it adopted in the Cross-Border Adopting Release.[53] The relief from the extension requirements of the tender offer rules may not be relied upon unless the bidder is eligible to rely on the Tier II exemption and the bidder undertakes not to waive or reduce the minimum acceptance condition below a majority or such percentage threshold required to control the target company under applicable foreign law, if greater. The Commission had initially proposed a simple majority threshold.

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50 *See* new Exchange Act Rule 14d-1(d)(2)(viii).
51 *Id.*
52 The Cross-Border Adopting Release, Section II.B.
53 *See* Section II.C.5 of the Release.

Furthermore, this interpretive position is limited to circumstances where there is a requirement of law or practice in the foreign home country justifying a bidder's inability to extend the offer or afford withdrawal rights after a waiver or reduction in the minimum offer condition, and does not apply to mandatory extensions under U.S. law for changes related to the offer consideration, the amount of target securities sought in the offer or a change to the dealer's soliciting fee. Bidders seeking to rely on this guidance, which is already effective as modified, will be required to disclose fully and discuss all of the implications of the potential waiver or reduction, including at the specific levels contemplated, in the offering materials.

6. Early Termination of the Initial Offering Period or a Voluntary Extension of the Initial Offering Period

Under specified circumstances, the Commission has granted relief to bidders requesting early termination of the initial offering period (or any voluntary extension of that period), which under U.S. tender offer rules must remain open for specified minimum time periods after a material change in the terms of an offer. Early termination of the initial offering period is not permitted, however, where U.S. rules require mandatory offer extensions for certain changes to the terms of an offer, including those arising from changes in the offer consideration, the dealer's soliciting fee, the percentage of target securities for which the offer is made or other material changes. Thus, bidders making any of these kinds of changes to the terms of a tender offer may not terminate an initial offering period (or any extension of that period) before the scheduled expiration of the mandatory extension.

Responding to positive feedback from commenters, the Commission revised its rules to codify the guidelines set forth in staff no-action precedent for cross-border tender offers regarding the ability to terminate early an initial offering period or a voluntary extension of that period, subject to the conditions set forth below.[54] Under new Rule 14d-1(d)(2)(ix), bidders in cross-border tender offers conducted under Tier II may terminate an initial offering period, including a voluntary extension of that period, if at the time the initial offering period and withdrawal rights end:

- the initial offering period has been open for at least 20 U.S. business days;

[54] The Commission emphasized that the revised rules do not permit early termination upon the waiver of an offer condition, pointing out that the rules mandate that a tender offer remain open for specified time periods after a material change in the terms of an offer, which would include the waiver of a material offer condition. The Commission notes that to the extent foreign law would permit a waiver of the offer conditions to trigger a requirement to immediately terminate the initial offering period or any voluntary extension of that period, the staff will continue to consider requests for relief on a case-by-case basis.

- the bidder has adequately discussed the possibility and the impact of the early termination in the original offer materials;
- the bidder provides a subsequent offering period after the termination of the initial offering period;
- all offer conditions are satisfied as of the time when the initial offering period ends; and
- the bidder does not terminate the initial offering period or any extension of that period during any mandatory extension required under U.S. tender offer rules.

The Commission is also amending Rule 13e-4 to add a new provision, Rule 13e-4(i)(2)(vii), to allow issuers or affiliates in a Tier II issuer tender offer to early terminate the initial offering period, or voluntary extension of that period, under the same circumstances discussed above.

7. Codification of Rule 14e-5 Cross-Border Exemptions

The Commission adopted the proposed amendments to Exchange Act Rule 14e-5, with some modifications, to codify recent exemptive relief issued for Tier II-eligible tender offers in the following three areas: purchases and arrangements to purchase securities of a foreign private issuer (1) pursuant to the non-U.S. tender offer(s) in a cross-border tender offer where there are separate U.S. and non-U.S. offers; (2) by offerors and their affiliates outside a tender offer; and (3) by financial advisors' affiliates outside a tender offer. Rule 14e-5 prohibits purchasing or arranging to purchase any subject securities or any related securities except as part of the tender offer and applies from the time of public announcement of the tender offer until the offer expires. The rule applies to "covered persons" as that term is defined in the rule.[55]

Amended Rule 14e-5(b)(11), which was adopted as proposed, permits purchases or arrangements to purchase pursuant to a foreign tender offer (or in more than one foreign offer) during the Rule 14e-5 prohibited period if certain conditions are satisfied. This exception permits purchases in a foreign offer or offers made concurrently or substantially concurrently with a U.S. offer under Rule 14d-1(d)(2)(ii). The tender offer must qualify as a Tier II tender offer under Rule 14d-1(d). The exception is also conditioned on the existence

[55] Covered persons include the offeror and its affiliates, the offeror's dealer-manager and its affiliates, any advisor to such persons and any person acting, directly or indirectly, in concert with such persons in connection with any purchase or arrangement to purchase any subject securities or any related securities.

of certain safeguards to help protect U.S. security holders.[56] For example, U.S. security holders must be treated at least as favorably as non-U.S. tendering security holders. The exception does not apply to open market transactions, private transactions or other transactions outside the tender offer.

Rule 14e-5(b)(12) was adopted as proposed, with one modification, and permits purchases or arrangements to purchase outside a Tier II tender offer by (i) an offeror and its affiliates and (ii) an affiliate of a financial advisor if certain conditions are satisfied. The Commission states that the revised rule is intended to address situations where the subject company is a foreign private issuer and the covered person *reasonably expects* that the tender offer qualifies as Tier II.[57] The revised rule prohibits any purchases or arrangements to purchase in the United States otherwise than pursuant to the tender offer.[58] Further, it contains conditions to enhance the transparency of the excepted activity. For example, the rule requires that the U.S. offering materials prominently disclose the possibility of or the intention to make purchases or arrangements to purchase outside the tender offer. The rule also requires disclosure in the United States of purchases made outside the tender offer to the extent that such information is made public in the subject company's home jurisdiction. Purchases or arrangements to purchase must be conducted in accordance with the applicable laws of the subject company's home jurisdiction.

Where an offeror or its affiliate purchases or arranges to purchase outside a tender offer, the exception imposes one additional condition regarding consideration. In order to safeguard against the disparate treatment of security holders, the exception requires that the tender offer price be raised to equal any higher price paid outside the tender offer.[59]

Where an affiliate of a financial advisor purchases or arranges to purchase outside a tender offer, the exception imposes additional conditions. The exception requires that the financial advisor and affiliate maintain and enforce written policies and procedures designed to prevent the flow of information between the financial advisor and the affiliate that might result in a violation of the federal securities laws and regulations. It also requires that the affiliate have no officers (or persons performing similar functions) or employees (other than clerical, ministerial, or support personnel) in common with the financial advisor that directly

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[56] *See* Section II.C.7 of the Proposing Release.

[57] The Commission noted in the Proposing Release that it would modify the reasonable expectation condition if the proposal to change the timing of the Tier II calculation to a date no earlier than 60 days before the tender offer announcement is adopted. However, although the Commission modified the reference date, it retained a reasonable expectation standard as it relates to such new date.

[58] The Commission confirmed in the Release that financial advisors and their affiliates should continue to be able to make purchases in the United States pursuant to other available exemptions.

[59] Prior relief granted by the Commission had required that the law of the applicable local jurisdiction itself require such an increase in the offer price to match any consideration paid outside the offer. This addition permits a bidder to *elect* to provide such treatment to have the benefit of the Rule 14e-5 exemption.

effect or recommend transactions in the subject securities or related securities who also will be involved in providing the offeror or subject company with financial advisory services or dealer-manager services. In addition, the financial advisor must have a registered broker-dealer affiliate under Section 15(a) of the Exchange Act. Finally, the exception does not permit purchases or arrangements to purchase to be made to facilitate the tender offer. Although there was language in the Proposing Release suggesting that purchasing activity effected in reliance on the exception would have to be consistent with the affiliate's prior levels of trading activity,[60] in the Release, the Commission clarified its position, stating that "[w]e acknowledge that the barometer for what constitutes the level of *normal* business activity may fluctuate once there is an announcement of a tender offer. However, if the level of purchasing activity far exceeds the usual or expected level of purchasing activity following the announcement of a tender offer, this could certainly be a red flag of improper facilitation."[61] Accordingly, it would be prudent to consider whether increases in trading activity following announcement of a tender offer call into question compliance with the amended rule.

The Commission determined not to adopt the proposal specifically to exclude risk arbitrage from the exception applicable to the financial advisor's affiliates.[62] The Commission notes that the general prohibition on activities designed to facilitate the tender offer should be sufficient to protect against abuse without a specific exclusion for risk arbitrage, which would in any event be difficult to define with precision.

The Commission's revised rules also have removed certain conditions to the availability of the exemptions that have been granted by the Commission from time to time to offerors, financial advisors and their respective affiliates through exemptive class letters, such as voluntary compliance by the financial advisor and its affiliates with the pertinent provisions of the United Kingdom's City Code on Takeovers and Mergers and Rules Governing Substantial Acquisition of Shares[63] and certain compliance requirements with the laws of the target's home jurisdiction and the existence of a bilateral or multilateral

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[60] The Proposing Release had indicated that "[a]s the exception is premised on the affiliate of the financial advisor carrying out its normal business activity when purchasing outside a tender offer, it would not permit purchases or arrangements to purchase to be made to facilitate the tender offer. Accordingly, purchasing activity effected in reliance on the proposed exception should be consistent with the affiliate's prior levels of activity." *See* Section II.C.7 of the Proposing Release.

[61] *See* Section II.C.7.b. of the Release.

[62] The Commission's proposed wholesale exclusion of risk arbitrage from the types of activities financial advisors' affiliates may conduct outside the tender offer was in fact a departure from the relief it previously granted in Rule 14e-5 Relief for Certain Trading Activities of Financial Advisors (April 4, 2007) (the "Financial Advisor Letter"), which did not contain such a flat prohibition. *See* Financial Advisor Letter and the attached request at page 3.

[63] *See* Condition number 10 in the Financial Advisor Letter.

memorandum of understanding.[64] The absence of these unnecessary conditions is a welcome improvement that promises to make the exemptions more useful to offerors, financial advisors and their affiliates.

8. Expanded Availability of Early Commencement for Exchange Offers

In 1999, as part of amendments to the tender offer rules separate from the cross-border amendments, the Commission adopted rule changes permitting exchange offers to commence upon the date of the filing of a registration statement under specified conditions to address the disparity in the regulatory process for cash tender offers (which could commence immediately upon filing of a tender offer statement) and exchange offers (which, prior to the 1999 rule revisions, could not commence until the staff completed its review of the registration statement and it had been declared effective).[65] Noting that the regulatory disparity continues to exist to some extent because the early commencement option is not available for exchange offers that are not subject to Rule 13e-4 or Regulation 14D, the Commission adopted rule changes expanding the availability of early commencement to *all* exchange offers, including those for domestic target companies not subject to Rule 13e-4 or Regulation 14D.[66]

Under the revised rules, offers not subject to Rule 13e-4 or Regulation 14D, such as those where the subject securities are not registered under Section 12 of the Exchange Act, may now commence before the effectiveness of a registration statement, but only under the same conditions as would offers subject to Exchange Act Rule 13e-4 or Regulation 14D. Amended Securities Act Rule 162(a) requires the bidder to provide withdrawal rights in the offer to the same extent as would be required under such rules. Amended Securities Act Rule 162(b) makes clear that the prospectus delivery requirements, including the requirement to deliver revised prospectuses and prospectus supplements contained in that provision, also will extend to offers not subject to Rule 13e-4 or Regulation 14D. In addition, if there is a material change in the information provided to target security holders, the revised rule would require the bidder to disseminate revised materials as required under Exchange Act Rules 13e-4(e)(3) and 14d-4(d) and to hold the offer open with withdrawal rights for the minimum time periods specified in those rules.

As noted above, the Commission also adopted a number of rule revisions that limit the need to provide withdrawal rights in Tier II cross-border tender offers, under the

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64 *See, e.g.*, Cash Tender Offer by Sulzer AG for the Ordinary Shares of Bodycote International plc (March 2, 2007) (cited in footnote 255 of the Release).

65 *See* SEC Release Nos. 33-7760; 34-42055 (October 22, 1999), Section II.E.1.

66 *See* amended Securities Act Rule 162(a) and (b).

circumstances outlined in the revised rules.[67] Offerors not subject to the provisions of Rule 13e-4 or Regulation 14D because, for example, the subject securities are not registered under Section 12 of the Exchange Act will be able to rely on the revised exemptions available for Tier II cross-border tender offers to the same extent as if the offers were subject to Rule 13e-4 or Regulation 14D. Similarly, bidders may rely on the modified interpretive position described above regarding the ability to waive or reduce a minimum acceptance condition without providing withdrawal rights.[68]

III. Beneficial Ownership Reporting by Foreign Institutions

The beneficial ownership reporting provisions require, subject to exceptions, that any person who acquires more than 5% of a class of voting equity securities registered under Section 12 of the Exchange Act report the acquisition on Schedule 13D within 10 days. Under certain circumstances, however, investors that have acquired the securities in the ordinary course of business without the purpose or effect of changing or influencing control of the issuer may qualify to file a short-form report on Schedule 13G instead of Schedule 13D. Utilization of Schedule 13G currently is available for such passive investments only if such investor is a U.S. bank as defined in Section 3(a)(6) of the Exchange Act, registered investment company or other specified type of U.S. institutional investor (a "qualified institutional investor")[69] or if the investor beneficially owns less than 20% of the outstanding voting equity securities (a "non-qualified passive investor").[70] Qualified institutional investors generally need not file their Schedule 13G until 45 days after the end of the

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[67] *See* new Exchange Act Rules 13e-4(i)(2)(vii) and 14d-1(d)(2)(ix) (allowing bidders to terminate an initial offering period immediately upon satisfaction of all offer conditions). *See* also new Exchange Act Rules 13e-4(i)(2)(v) and 14d-1(d)(2)(vii) (permitting suspension of back-end withdrawal rights while securities are being counted).

[68] The Commission notes that these rule changes will significantly expand the universe of exchange offers that may commence early, which could result in an increased burden on the staff to complete the review process for such offers on an expedited basis, as it had committed to do in 1999 in an effort to equalize the regulatory treatment of cash versus stock tender offers. While the Commission indicated that it intends to continue to afford expedited treatment for these filings, the review process may be somewhat longer in cases involving novel or unusually complex issues, such as exchange offers where the bidder is registering its initial public offering.

[69] *See* Rule 13d-1(b) under the Exchange Act. As specified in Rule 13d-1(b)(1)(ii), the types of institutional investors that may file on Schedule 13G under that rule include a broker or dealer registered under Section 15 of the Exchange Act, a bank as defined in Section 3(a)(6) of the Exchange Act, an insurance company as defined in Section 3(a)(19) of the Exchange Act, an investment company registered under Section 8 of the Investment Company Act of 1940 (the "Investment Company Act"), an investment adviser registered under Section 203 of the Investment Advisers Act of 1940 or under the laws of any state, an employee benefit plan or pension fund that is subject to the provisions of the Employee Retirement Income Security Act of 1974, a savings association as defined in Section 3(b) of the Federal Deposit Insurance Act of 1950, a church plan that is excluded from the definition of an investment company under Section 3(c)(14) of the Investment Company Act, and related holding companies and groups.

[70] *See* Rule 13d-1(c) under the Exchange Act.

calendar year in which the acquisition occurred, and only if they remain above the 5% threshold at the end of the calendar year. Non-qualified passive investors must file their Schedule 13G within the same period as a Schedule 13D would be due, *i.e.*, within 10 calendar days of crossing the threshold.

The Commission adopted amendments to extend Schedule 13G filing eligibility based on the qualified institutional investor exception to include foreign institutions that are *substantially comparable* to the U.S. institutions listed in the current rule.[71] To be eligible to file on Schedule 13G as a qualified institutional investor, the foreign institution is required to determine, and to certify on Schedule 13G, that it is subject to a regulatory scheme substantially comparable to the regulatory scheme applicable to its U.S. counterparts. In addition, the foreign institution would need to undertake, in its certification on Schedule 13G, to furnish to the Commission staff, upon request, the information it otherwise would be required to provide in a Schedule 13D.

Amended Rule 13d-1(b) is available only to institutions that acquire and hold equity securities in the ordinary course of business and not with the purpose or effect of influencing or changing control of the issuer. In the event that an institution – foreign or domestic – determines that it holds subject securities with a disqualifying purpose or effect, it is required to file a Schedule 13D as set forth in Rule 13d-1(e) no later than 10 calendar days after the change in investment purpose. In addition, such institution is subject to a "cooling-off period," during which time the reporting person is prohibited from voting or directing the voting of the subject securities or acquiring additional beneficial ownership of any equity securities of the issuer or any person controlling the issuer.

A foreign institutional investor that is currently filing on Schedule 13G in reliance upon a prior no-action letter received from the staff may continue to do so to the extent it continues to meet the conditions upon which the no-action relief was granted. However, when these institutions otherwise would be required to file an amendment to the Schedule 13G, or in the case of a new filing on Schedule 13G, they must provide the certification required under the revised rule to file on that Schedule.

The Commission also adopted a corresponding change to Exchange Act Rule 16a-1(a)(1) to include the foreign institutions eligible to rely on the qualified institutional investor exception described above. Rule 16a-1(a) sets forth the definition of beneficial ownership for purposes of determining who is a more than 10% beneficial owner under Exchange Act Section 16. Rule 16a-1(a)(1) allows the institutions identified in the rule to exclude from beneficial ownership calculations the shares they hold for the benefit of third parties or in customer or fiduciary accounts in the ordinary course of business, without the purpose or effect of changing control of the issuer, or in connection with or as a participant

[71] *See* new Rule 13d-1(b)(1)(ii)(J).

in any transaction that has such a purpose or effect, including any transaction subject to Rule 13d-3(b). Therefore, these institutions typically will not be 10% owners subject to Section 16(a) reporting, Section 16(b) short-swing profit recovery and Section 16(c) restrictions on short sales.

IV. Commission Interpretive Guidance

In addition to the rule changes and interpretive guidance discussed above, the Release includes Commission guidance on the following issues:

- the application of the all-holders provisions of the tender offer rules to foreign target security holders;
- the ability of non-U.S. bidders to exclude U.S. target security holders in cross-border tender offers; and
- the ability of non-U.S. bidders to use the vendor placement procedure for cross-border exchange offers.

A. Application of the All-Holders Rule to Foreign Target Security Holders

In 1986, the Commission adopted Rule 14d-10 and amended Rule 13e-4(f) to require that all target security holders in a tender offer subject to either of those rules be included in the tender offer and treated equally.[72] These rules require, with narrow exceptions, that third-party tender offers subject to Section 14(d) of the Exchange Act, as well as issuer tender offers subject to Section 13(e) of the Exchange Act, be open to all holders of the subject class of securities. This equal treatment provision does not prohibit tender offers for less than all outstanding securities of a subject class, but it does require that all security holders be able to accept the tender offer if they choose. Implicitly, the all-holders provisions in Rules 14d-10 and 13e-4(f) apply equally to U.S. and non-U.S. target holders.

The Commission reiterated its position that the all-holders requirement does not allow the exclusion of any foreign or U.S. target holder in tender offers subject to those rules. The Commission notes in the Release that it recognizes the requirement to make an offer available to all foreign target holders, particularly for registered exchange offers, may present a burden for bidders that may need to comply with both foreign and U.S. rules. The Commission was not swayed by arguments from commenters that the burden of ensuring the inclusion of foreign holders in U.S. tender offers outweighs any benefit in protecting those foreign holders, whose protection properly resides within the purview of the foreign

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[72] *See* Amendments to Tender Offer Rules: All-Holders and Best-Price, Release No. 34-23421 (July 11, 1986).

regulator. The Commission states that it is in the interest of U.S. investors to enforce U.S. equal treatment principles for the benefit of non-U.S. target security holders, particularly where comparable foreign all-holders requirements may protect U.S. investors by preventing their exclusion from cross-border offers. The Commission declined to adopt a de minimis or other exception to the U.S. equal treatment provisions despite suggestions from some commenters to allow exceptions in certain circumstances. The Commission indicated its intention to monitor this issue with respect to future tender offers to determine whether further Commission action is needed.

Notwithstanding the requirements of Rule 14d-10 and Rule 13e-4(f) to extend an offer to all holders of a target company's securities, the Commission clarifies that these provisions have not been interpreted to require that offering materials be mailed into foreign jurisdictions. In addition, noting that certain bidders have required target holders to certify that tendering their securities complies with local laws or that an exemption applies that allows such tenders without further action by the bidder to register or qualify its offer, the Commission states that it does not believe it is appropriate to shift this burden of assuring compliance with the relevant jurisdiction's laws to target security holders, because target security holders may not be in possession of relevant facts regarding the bidder's action and the provisions of local law in their home jurisdiction necessary to make this determination.

B. Ability of Non-U.S. Bidders to Exclude U.S. Target Security Holders

The Commission also provides additional guidance in the Release on whether and how non-U.S. bidders in cross-border business combination transactions legitimately may avoid the application of U.S. registration and tender offer rules. Whether U.S. tender offer rules apply in the context of a cross-border tender offer depends on whether the bidder uses U.S. jurisdictional means in making a tender offer. The Commission has provided guidance on measures non-U.S. acquirors may take to avoid using U.S. jurisdictional means through previously issued releases.[73] The guidance expressed in the Release supplements the guidance in those releases. The Commission emphasizes that with the expansion of the cross-border exemptions under the new rules, there should be fewer circumstances warranting exclusionary offers, because it will be easier to balance the regulatory requirements of foreign and U.S. rules.

The Commission reiterates that a legend or disclaimer stating that the offer is not being made into the United States, or that the offer materials may not be distributed there, is not likely to be sufficient in itself, because if the bidder wants to support a claim that the

[73] *See generally* Statement of the Commission Regarding Use of Internet Web Sites to Offer Securities, Solicit Securities Transactions or Advertise Investment Securities Offshore, Release Nos. 33-7516; 34-39779 (March 23, 1998) (the "1998 Internet Release") and the Cross-Border Adopting Release.

offer has no jurisdictional connection to the United States, it also will need to take special precautions to prevent tenders from U.S. target holders.

The Commission also points out that bidders may require a representation or certification from tendering holders that they are not U.S. holders to avoid application of U.S. law. The Commission recognizes the possibility that target security holders could misrepresent their status in order to be permitted to tender into an exclusionary offer. The Commission has previously stated that where this occurs, bidders will not be viewed as having targeted U.S. investors, thereby invoking U.S. jurisdictional means.[74] However, the Commission clarifies that this position is premised on the bidder's having taken adequate measures reasonably designed to guard against purchases from U.S. holders. It is also premised on the absence of indicia, such as payment drawn on a U.S. bank or provision of a U.S. taxpayer identification number, that would or should put the bidder on notice that the tendering holder is a U.S. investor.

The Commission did not discuss the implication of the target's conduct on a bidder's attempt to avoid the use of U.S. jurisdictional means.[75]

The Commission indicates in the Release that in the future it will more closely monitor exclusionary offers to determine whether Commission action is necessary to protect U.S. target holders.

C. Vendor Placements

The Release includes an interpretive section discussing the Commission's views on the use of vendor placement structures in cross-border exchange offers. In a vendor placement, the bidder typically employs a third party to sell in offshore transactions the securities to which tendering U.S. target holders would be entitled in the offer. The bidder (or the third party) then remits the proceeds of the resale (minus expenses) to those U.S. target holders that tendered into the offer.

Vendor placements raise two potential issues under U.S. federal securities laws. The first is whether securities issued and sold offshore on behalf of U.S. holders require Securities Act registration. Second, in those exchange offers subject to Section 13(e) or 14(d) of the Exchange Act – essentially, offers for registered equity securities – the question is whether the equal treatment provisions of the U.S. tender offer rules allow the bidder to offer U.S. target holders a different form of consideration (cash) than what is provided to

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[74] *See* Section III.C of the 1998 Internet Release.

[75] *Cf. Plessey Co. plc v. General Electric Co. plc*, 628 F. Supp. 477 (D. Del. 1986), holding that the bidder did not have to comply with the tender offer rules under the Exchange Act when the *target* made use of U.S. jurisdictional means.

foreign target holders (securities), or to offer certain U.S. holders for which a Securities Act exemption is available (*e.g.*, accredited investors or qualified institutional buyers) securities, while offering other U.S. holders cash.

With respect to registration requirements under Section 5 of the Securities Act, the Commission indicates that it no longer intends to issue vendor placement no-action letters. However, the Commission reiterates that vendor placements may be used without violating Section 5, provided that bidders follow the guidance set forth in previous no-action letters.[76] The factors include:

- the level of U.S. ownership in the target company;
- the number of bidder securities to be issued in the business combination transaction as a whole compared to the amount of bidder securities outstanding before the offer;
- the amount of bidder securities to be issued to tendering U.S. holders and subject to the vendor placement, compared to the amount of bidder securities outstanding before the offer;
- the liquidity and general trading market of the bidder's securities;
- the likelihood that the vendor placement can be effected within a very short period of time (*i.e.*, within a few business days) after the termination of the offer and the bidder's acceptance of shares tendered in the offer;
- the likelihood that the bidder plans to disclose material information, such as earnings results, forecasts or other financial or operating information, around the time of the vendor placement sales; and
- the process used to effect the vendor placement sales, such as whether the vendor placement involves special selling efforts by brokers or others acting on behalf of the bidder.

While all factors are relevant to the analysis, two are particularly salient – market liquidity and the relative amount of securities going to U.S. holders. Generally, except where both the market for the bidder securities is highly liquid and the amount of bidder securities

[76] *See, e.g.*, Singapore Telecommunications Ltd. (May 15, 2001); Oldcastle, Inc. (July 3, 1986); Hudson Bay Mining and Smelting Co., Ltd. (June 19, 1985); Getty Oil (Canadian Operations) Ltd. (May 19, 1983); Equitable Life Mortgage and Realty Investors (December 23, 1982); and Electrocomponents PLC (September 23, 1982) (cited in footnote 360 of the Release).

issued to U.S. target holders is small relative to the total amount of bidder securities outstanding, the Commission would consider Securities Act registration to be required. The Commission is also concerned with the level of U.S. ownership in the target company, even though it is not necessarily indicative of a high percentage of bidder securities going to U.S. holders. Indeed, in both the Proposing Release and the Release, the Commission states that offerors should be "particularly cognizant" of this factor.[77]

In addition to determining whether securities issued and sold offshore on behalf of U.S. holders require Securities Act registration, a second issue to consider is whether the tender offer is subject to Section 13(e) or 14(d) of the Exchange Act. If so, and if the Tier I exemption is not available, bidders will need to seek an exemption from the equal treatment requirements in order to offer U.S. holders a different form of consideration than non-U.S. holders. The Commission indicates that its staff will consider requests for relief from these provisions where vendor placement procedures are used. However, it has done so only once before, in response to TABCORP, an Australian company, approximately 17% of the ordinary shares of which was beneficially owned by U.S. holders.[78] This suggests that while the staff will entertain requests for this type of relief, bidders should not expect it to be lightly granted.

In sum, the use of vendor placement procedures for cross-border tender offers remains viable, mainly for offers in which the target securities are not listed in the United States and where the facts and circumstances of the offer align with the factors described above.

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Please feel free to contact any of your regular contacts at the firm or any of our partners and counsel listed under Mergers, Acquisitions and Joint Ventures or Capital Markets in the "Practices" section of our website (http://www.clearygottlieb.com) if you have any questions.

CLEARY GOTTLIEB STEEN & HAMILTON LLP

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[77] *See* Section II.G.3 of the Proposing Release; footnote 362 of the Release. The Commission has not provided specific guidance regarding the maximum level of U.S. ownership in target companies it is prepared to permit. In a recent call with the staff of the Division of Corporation Finance, we were advised that the staff considers U.S. ownership levels below 20% generally to be acceptable; would recommend consultation with the staff at U.S. ownership levels of 20%-30%; and is unlikely to view U.S. ownership levels above 30% as acceptable.

[78] *See* TABCORP Holdings Ltd. (August 20, 1999) (cited in footnote 368 of the Release).

NEW YORK
One Liberty Plaza
New York, NY 10006-1470
1 212 225 2000
1 212 225 3999 Fax

WASHINGTON
2000 Pennsylvania Avenue, NW
Washington, DC 20006-1801
1 202 974 1500
1 202 974 1999 Fax

PARIS
12, rue de Tilsitt
75008 Paris, France
33 1 40 74 68 00
33 1 40 74 68 88 Fax

BRUSSELS
Rue de la Loi 57
1040 Brussels, Belgium
32 2 287 2000
32 2 231 1661 Fax

LONDON
City Place House
55 Basinghall Street
London EC2V 5EH, England
44 20 7614 2200
44 20 7600 1698 Fax

MOSCOW
Cleary Gottlieb Steen & Hamilton LLP
CGS&H Limited Liability Company
Paveletskaya Square 2/3
Moscow, Russia 115054
7 495 660 8500
7 495 660 8505 Fax

FRANKFURT
Main Tower
Neue Mainzer Strasse 52
60311 Frankfurt am Main, Germany
49 69 97103 0
49 69 97103 199 Fax

COLOGNE
Theodor-Heuss-Ring 9
50668 Cologne, Germany
49 221 80040 0
49 221 80040 199 Fax

ROME
Piazza di Spagna 15
00187 Rome, Italy
39 06 69 52 21
39 06 69 20 06 65 Fax

MILAN
Via San Paolo 7
20121 Milan, Italy
39 02 72 60 81
39 02 86 98 44 40 Fax

HONG KONG
Bank of China Tower
One Garden Road
Hong Kong
852 2521 4122
852 2845 9026 Fax

BEIJING
Twin Towers – West
12 B Jianguomen Wai Da Jie
Chaoyang District
Beijing 100022, China
86 10 5920 1000
86 10 5879 3902 Fax