New ways to cross the border

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Tier I and Tier II Exemptions

The Amendments include the following changes to the existing Tier I and Tier II Exemptions, which primarily codify prior SEC exemptive and no-action relief in order to reduce the conflict between US tender offer rules and non-US takeover regulations:

- *Expanding exemptive relief to the going private rules*. Before the Amendments, the Tier I and Rule 802 Exemptions provided relief from the registration and disclosure requirements only for particular types of affiliated transactions. This limitation conflicted with common overseas acquisition structures. After the Amendments, any form of transaction that satisfies the conditions of the Tier I or Rule 802 Exemptions will be exempt from the application of Exchange Act Rule 13e-3 (which requires substantial additional disclosures related to the procedural fairness of the transaction). As a result, cross-border cash mergers, compulsory acquisitions for cash, and schemes of arrangement, in addition to tender offers and merger transactions, can benefit from the Cross-Border Rules.

- *Extending the exemption to unregistered offerings*. The Amendments extend the availability of the Tier II Exemption to unregistered tender offers (tender offers for securities that are not registered under Exchange Act Section 12 and subject only to Regulation 14E of the Exchange Act, other than the prompt payment, extension, and notice-of-extension requirements, which are already excepted by the Tier II Exemption).

- *Permitting multiple foreign offers*. Prior to the Amendments, the Tier II Exemption permitted an acquiror to separate an offer into a US offer and a non-US offer without violating the "all holders" rule, so long as the US offer was made on terms at least as favorable as the non-US offer. The SEC received various requests to permit an acquiror to conduct multiple overseas offers because a literal reading of the Tier II Exemption suggested that only two tender offers could be made (the US and non-US offer). The SEC eliminated this strict interpretation under the Amendments by specifying that an acquiror can conduct multiple foreign tender offers (as opposed to just one) contemporaneously with a US tender offer.

- *Opening domestic offers to all ADR holders and foreign offers to US shareholders*. Before the Amendments, a multiple tender offer scheme relying on the Tier II Exemption could extend the US offer only to US persons and the non-US offer only to non-US persons. This limitation created transaction issues because an acquiror typically wanted, for efficiency reasons, the US offer extended to all holders (regardless of nationality) of the target's American Depositary Receipts, and some foreign takeover laws prohibited the exclusion of any shareholder from a tender offer (so the requirement under the Tier II Exemption to exclude US shareholders from a non-US offer created a regulatory conflict). The Amendments ease these participation rules by allowing an acquiror conducting a cross-border transaction with multiple tender offers, one of which is a concurrent US tender offer pursuant to the Tier II Exemption, to make: (1) the US offer available to *all* holders of the target's American Depositary Receipts, including non-US shareholders (but not to non-US shareholders who do not own shares in ADR

form); and (2) the foreign offer available to US shareholders (but does not require that US shareholders must tender into the foreign offer), so long as the laws of the target's home jurisdiction expressly prohibit the exclusion of any shareholder from an offer and the offering materials distributed to US target shareholders describe the risks to US shareholders of participating in the non-US offer.

- *Terminating back-end withdrawal rights while tendered securities are counted.* US tender offer rules require that tendering shareholders for Exchange Act registered securities be provided with withdrawal rights from the start of the tender offer until the subject shares have been accepted for payment. This provides shareholders with "back-end" withdrawal rights since they can still withdraw their shares pending payment after an initial offering period has closed. Back-end withdrawal rights can result in conflicts with foreign takeover laws because in many overseas jurisdictions the counting of tendered securities after the close of the initial offering period can take a substantial amount of time, so if shareholders are entitled to withdraw their shares after the close of an initial offering period, then uncertainty could exist whether a minimum tender condition has been satisfied. Pursuant to the Amendments, an acquiror can suspend withdrawal rights after the expiration of a tender offer while tendered securities are being counted and before they have been accepted for payment (even if no subsequent offering period is provided), so long as: (1) the offer period (which includes withdrawal rights) is at least 20 US business days; (2) at the time withdrawal rights are suspended, all offer conditions (other than the minimum acceptance condition, and only that condition) have been satisfied or waived; and (3) back-end withdrawal rights are suspended only until tendered securities are counted and are reinstated immediately thereafter (unless the securities have been accepted).

- *Extending relief for payment schemes in cross-border subsequent offers*. With respect to subsequent offering periods for cross-border tender offers relying on the Tier II Exemption, an acquiror can: (1) bundle and pay for securities tendered in a subsequent offering period as promptly as possible within 20 business days of the date of tender (rather than pay on a rolling basis, as mandated for domestic offers); (2) pay interest at statutory rates on securities tendered during a subsequent offering period (without violating the all-holders rule under Exchange Act Rule 14d-10) if such payment is required by the laws of the target's home jurisdiction; and (3) use separate offset pools for securities tendered during the initial and subsequent offering periods, and include a ceiling for the form of alternate consideration proffered in a "mix and match" offer structure.

In a "mix and match" offer, an acquirer offers a set mix of cash and securities in exchange for each target share, but permits tendering holders to request a different proportion of cash or securities, with the aim that elections by tendering shareholders will be satisfied to the extent that other tendering shareholders make offsetting elections for the opposite proportion of cash and securities. U.S. tender offer rules conflict with mix and match offers and require relief under the Amendments since U.S. tender offer rules: (i) allow a choice of different forms of consideration in a subsequent offering period only if there is no cap on the forms of consideration (but the prohibition on a cap is inconsistent with the offset feature of mix and match offers); and (ii) require that the same form and amount of consideration be offered to tendering shareholders in both the initial and subsequent offering periods (but two pro-ration and offset pools would need to be created—one for securities tendered during the initial offering period and one for securities tendered during the subsequent offering period—because U.S. prompt payment rules require that elections of tendering shareholders in the initial offering must be aggregated and offset against each other before the commencement of the subsequent offering period).

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- *Terminating withdrawal rights after the reduction or waiver of the minimum acceptance condition.* US tender offer rules require an acquiror to keep its offer open for specified periods of time after a material change has been made to the offer terms. During this extension period, the acquiror must provide withdrawal rights. Under the Cross-Border Original Release, the SEC provided interpretative guidance allowing an acquiror to waive or reduce the minimum acceptance condition without providing withdrawal rights if certain conditions were met. Without such relief, a reduction or waiver of a minimum acceptance condition would constitute a material change to the offering, requiring a mandatory extension of the offer since it could influence the investment decisions of both target shareholders who have tendered and those who have not yet tendered. The SEC stated in the Cross-Border Amendments Release that its prior interpretative guidance was being extended in contexts it did not intend. Accordingly, an acquiror conducting a cross-border tender offer relying on the Tier II Exemption can waive or reduce a minimum acceptance condition without providing withdrawal rights only if more stringent conditions are met.

- *Accelerating the expiration of an offering period.* An acquiror can accelerate the expiration date of a cross-border tender offer relying on the Tier II Exemption (either during the initial offering period or a voluntary extension of that period) and not provide withdrawal rights if as of the requested expiration time of the offering period: (1) the initial offering period has been open for at least 20 U.S. business days and all offer conditions have been satisfied (and not waived); (2) the acquiror's offering documents adequately discuss the possibility and the impact of the potential for an early expiration of the offering period; (3) the acquiror provides a subsequent offering period after the early expiration of the initial offering period; and (4) the acquiror does not terminate the offering period during any mandatory extension specified under US tender offer rules. (*See* Exchange Act Rules 13e-4(e)(3), 14d-4(d)(2) and 14e-1(b) for the circumstances that require a mandatory extension of an offer under U.S. tender offer rules)..The Amendments do not permit an early expiration upon the waiver of an offer condition. When an acquiror waives an offer condition, the terms of the offer may be fundamentally modified, which could influence the investment decision of shareholders who have already tendered and those who have not yet tendered. On the other hand, the SEC believes that if all offer conditions have been satisfied, such change is less fundamental since target shareholders should know from the beginning of the offer of the possibility that all offer conditions could be successfully satisfied at some point during the offer period. Although the minimum time periods during which an offer must remain open after a notice of a material change in its terms is communicated to target shareholders are applicable only to early commenced exchange offers, the SEC has stated that it views these time periods as applicable to all tender offers, including those subject only to Regulation 14E under the Exchange Act.

- *Expanding the ability to purchase target stock outside the tender offer.* Exchange Act Rule 14e-5 does not allow "covered persons" (which includes the acquiror and its affiliates) from purchasing or arranging to purchase the target's subject equity securities outside of the tender offer. This restriction may conflict with foreign law or practice where purchases outside a tender offer are customary. To address this conflict, the Amendments codify SEC blanket no-action relief granted in three situations from 2006 to 2007 to permit the subject shares of a foreign private issuer target to be purchased outside a tender offer relying on the Tier II Exemption without violating Exchange Act Rule 14e-5 (1) by an acquiror if there are separate US and non-US offers (subject to certain safeguards addressing the economic terms, consideration,

and procedural terms of the tender offer); (2) by an acquiror and its affiliates (subject to certain conditions, including that the purchases are made outside the United States, public disclosures in the United States match disclosures made in the target's home jurisdiction regarding the amount of target stock purchased outside the tender offer, and the tender offer price is increased to match any consideration paid outside of the tender offer that is greater than the tender offer price); and (3) by a financial advisor's affiliates (subject to certain conditions that are in addition to those applicable to acquisitions by an acquiror and its affiliates, including that the financial advisor has established information barriers to prevent the transfer of material non-public information from the financial advisor to the trading affiliate, and the financial advisor has an affiliate that is registered as a broker or dealer under the Exchange Act). By requiring that the financial advisor has an affiliate that is registered as a broker or dealer under Exchange Act Section 15(a), an acquiror may find it objectionable and abandon a transaction (or exclude US target security holders) due to the need to replace or obtain additional advisors in order to benefit from the exemption.

Amendments that impact both domestic and cross-border tender offers

The Amendments include the following changes that apply both to domestic tender offers involving a US acquiror and a US target, as well as to cross-border tender offers relying on either the Tier I or Tier II Exemptions:

- *Eliminating the maximum length of subsequent offering periods*. With respect to subsequent offering periods for *both* US tender offers and cross-border tender offers relying on the Tier II Exemption, the current 20 US business day limit on the maximum length of subsequent offering periods will no longer apply. The requirement that the subsequent offering period be open for at least three U.S. business days continues to apply.

- *Expanding the availability of early commencement for exchange offers*. To reduce the regulatory disparity between cash and stock tender offers, the SEC previously adopted rules in 1999 permitting exchange offers subject to Exchange Act Rule 13e-4 or Regulation 14D of the Exchange Act to start on the date of the filing of a registration statement. The prior rules did not allow an acquiror to take advantage of the early commencement option if the subject securities were not subject to Regulation 14D of the Exchange Act or Exchange Act Rule 13e-4. The Amendments eliminate this distinction by permitting all exchange offers (both domestic and cross-border) subject to Regulation 14E of the Exchange Act to commence upon the filing of the registration statement registering the offer, so long as: (1) the offer is not an Exchange Act Rule 13e-3 going-private transaction or a roll-up transaction as described in Item 901 of Regulation S-K; (2) if there is a material change in the information provided to target security holders, then the acquiror disseminates revised offering materials and holds the offer open with withdrawal rights for the minimum periods specified in Exchange Act Rules 13e-4(e)(3) and 14d-4(d); (3) the acquiror provides withdrawal rights to the same extent as would be permitted under Exchange Act Rule 13e-4 and Regulation 14D of the Exchange Act; and (4) no target securities are actually purchased until the registration statement is declared effective by the SEC.

Form changes and issuance of interpretive guidance

Form changes. The Amendments include important procedural changes that impact the manner and contents of information furnished to the SEC. In particular, no longer will paper submissions be permitted and Forms CB and F-X must be furnished to the SEC electronically through the SEC's EDGAR system. Form F-X should be filed with the SEC at the time of the first Form CB submission. In addition, the SEC adopted changes to Schedule TO and Forms F-4 and S-4 to include boxes on the cover page of the forms that a filing person must check to

indicate whether reliance is being made on one or more exemptions under the Cross-Border Rules.

Interpretative guidance. The Amendments also include interpretive guidance from the SEC (a reminder of the SEC's position on a matter and not necessarily new thinking or a change in SEC interpretation) on the following issues:

- *Ability to exclude non-US shareholders from a domestic transaction.* In general, US tender offer rules require that any third-party tender offer or issuer self-tender for a security registered under Exchange Act Section 12 must be open to all shareholders of the subject class and all such shareholders must be treated equally. The foregoing "all-holders" requirement does not allow the exclusion of any US or foreign target shareholder in a tender offer subject to its provisions. However, the SEC reiterates its position that compliance with the all-holders requirement does not obligate a third-party acquiror or an issuer to disseminate offer materials outside the United States and special circumstances may exist that permit unequal access to non-US shareholders (foreign ownership restrictions may apply over the target or onerous registration requirements may exist in an overseas jurisdiction that may necessitate unequal treatment).

- *Ability to exclude US shareholders from a cross-border transaction.* The SEC recognizes that an overseas acquiror may have legitimate reasons to exclude US target shareholders from a cross-border transaction, and the Amendments reiterate prior guidance on how an acquiror in a cross-border transaction may lawfully avoid the application of US registration and tender offer rules. When an acquiror makes an exclusionary offer, the SEC believes that the acquiror must take appropriate measures to avoid the application of US jurisdictional means. The SEC explicitly warns that exclusionary offers will be viewed with scepticism if the target's stock trades over a US stock exchange and the participation of US shareholders is necessary to meet the minimum condition. Furthermore, the SEC cautioned that placing a legend or disclaimer stating that a tender offer is not being made into the United States or that materials may not be distributed there is not likely to be sufficient because an acquiror is required to take pro-active measures to prevent sales to or tenders from US target shareholders.

- *Ability to use vendor placements.* A vendor placement is a procedure designed to extend offers into the US without subjecting the transaction to the registration requirements of the Securities Act. While there is no standard structure to effect a vendor placement, the typical arrangement calls for the shares of the acquiror that accepting US target shareholders would have received in the offer be delivered to a trustee located outside of the United States. The trustee promptly sells such stock of the acquiror on the principal securities exchange on which the acquiror's stock trades, with the cash proceeds from such sale (net of the costs and expenses associated with the sale) remitted to US target shareholders as consideration for their acceptance of the offer. Although the Tier I Exemption allows an acquiror to provide target shareholders with different consideration (a cash-only alternative) an acquiror may prefer to use a vendor placement if it does not have sufficient cash to finance the transaction (as the acquiror's stock is sold under a vendor placement to fund the cash payments to US target shareholders), or the target's home jurisdiction requires that all target shareholders be offered the same consideration. Effecting a vendor placement is most practical if the acquiror is a "Category 1" issuer under Regulation S of the Securities Act, since there are no offering restrictions or notice requirements during the distribution compliance period.

Vendor placements raise two issues under US federal securities laws: (1) do the securities sold offshore on behalf of US target shareholders trigger the application of the registration requirements of the Securities Act, and (2) do the equal treatment provisions of US

tender offer rules prevent US target shareholders from receiving cash while other shareholders receive acquiror stock?

A typical vendor placement may trigger the application of US federal securities laws because an offer for the acquiror's stock is technically made to US target shareholders, even though cash instead of securities is ultimately delivered to accepting US target shareholders. The SEC has granted no-action letter relief from the registration requirements of the Securities Act based on arguments that requiring registration statement-type disclosures would not be relevant to accepting US target shareholders' investment decisions, as such persons would not have an ongoing interest in the stock of the acquiror. The Amendments expand upon this rationale and list the factors that the SEC will consider when assessing whether a vendor placement obviates the need for Securities Act registration. The SEC states that the information resulting from such factors will be used to evaluate whether US target shareholders are making an investment decision with respect to a purchase of securities (which would trigger registration pursuant to Securities Act Section 5) or making a decision to tender their target securities in exchange for cash (which may not be a fixed amount, but can be readily determined and estimated based on historic trading prices).

The SEC also suggests that vendor placements can be used in only very limited circumstances because it would not be appropriate in offers subject to the equal treatment provisions/all-holders requirements of US tender offer rules (such as an offer made pursuant to the Tier II Exemption) to: (1) provide U.S. target shareholders with only cash and other target shareholders with shares of the acquiror; (2) exclude all US target shareholders other than those US target shareholders for whom an exemption would be available from the registration requirements of Securities Act Section 5 (such as large institutional investors); or (3) issue securities to large institutional U.S. shareholders while providing cash to all other U.S. shareholders pursuant to a vendor placement arrangement. Under such circumstances, an acquiror would need to obtain exemptive relief from the SEC, which the SEC has rarely granted.

The Amendments do not provide a new regulatory approach to cross-border transactions. While the Amendments should increase regulatory certainty concerning recurring conflicts in the application of the Tier II Exemption to certain cross-border business combinations, the revised rules as a whole may not meet the SEC's target of encouraging overseas acquirors to extend more transactions into the United States, due to the methods used to calculate and determine the ownership level of US target security holders. The SEC's continued reliance on the look-through analysis, along with its retention of a 10% US security holder ownership threshold, are both substantial obstacles for overseas acquirors and discourage compliance with the Cross-Border Rules. Furthermore, determining the status of a US target security holder based on residency can lead to counter-intuitive results.

Overseas acquirors who are potentially eligible to rely on the Tier I or Rule 802 Exemptions may continue to lack incentive to use them even after the adoption of the Amendments because the small incremental number of shares to which they gain access by utilizing either exemption may not outweigh the time, cost, and uncertainty involved in conducting a look-through analysis. Because eligibility remains set at only 10%, the inclusion of US target security holders normally will have only a marginal impact on the success of the transaction, but extending an offer into the United States could expose the transaction parties to time delays, SEC intervention, and confidentiality leaks that could potentially derail the entire deal. In addition, US securities laws examine the residency of the security holder and not the particular capital market in which the security holder acquired the target's securities. As a result, a target security holder who acquired a target security while outside of the United States, but

subsequently relocated to the United States, would be considered a US security holder for purposes of calculating the eligibility requirements under the Cross-Border Rules, even though the target may never have directly accessed the US capital markets. When U.S. investors purchase securities issued overseas, they should have made their investment decision based on the issuer's home market disclosure documents (and not SEC-mandated disclosure) and they should rightly become subject to the applicable rules and regulations of the issuer's home market.

As the SEC is considering the future of US securities regulation for the 21st century, it may wish to again consider how to address the need to further encourage the extension of overseas offers to US security holders with fewer regulatory burdens. This need is accentuated when an acquiror is required by non-US law to extend its offer to all target security holders or the existence of U.S. security holders is not a result of the target accessing the US capital markets.. If a company's ability to effect its business plans outside the United States is curtailed when US persons own its securities, then foreign private issuers may opt to curb the offering of securities to US persons or restrict the ability of security holders to transfer securities to US persons. If enough foreign private issuers adopt either of these approaches, then the status of the US capital markets as the seat of global finance could be challenged.