SEC ADOPTS EXEMPTIONS FOR CROSS-BORDER TENDER OFFERS, EXCHANGE OFFERS AND RIGHTS OFFERINGS

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On October 22, 1999, the U.S. Securities and Exchange Commission (the "SEC") issued a release[1] (the "Release") adopting rule changes facilitating the extension of cross-border tender offers, exchange offers and rights offerings to U.S. investors. The SEC's new rules are similar to the rules that the SEC proposed in its proposing release[2] (the "Proposing Release") issued in November 1998 but have been revised in certain significant respects. The new rules will generally become effective on January 24, 2000.

The SEC's action seeks to address the concern that U.S. investors in securities of foreign private issuers have often been denied the opportunity to participate in tender offers, exchange offers and rights offerings relating to such securities. Offerors have frequently excluded U.S. investors from such transactions in order to avoid the onerous application of U.S. securities laws. By adopting the new rules, the SEC has relaxed the compliance burden placed on persons extending tender offers, exchange offers or rights offerings to U.S. holders.

The rules adopted in the Release provide five new exemptions from the full application of the U.S. securities laws:

- First, the new "Tier I" exemption exempts tender offers and exchange offers for securities of a foreign private issuer from most of the applicable provisions of the Securities Exchange Act of 1934 (the "Exchange Act") and rules thereunder governing such offers if U.S. holders own 10 percent or less[3] of the securities subject to the offer. This exemption is available to both U.S. and foreign bidders.

1. SEC Release No. 33-7759, 34-42054, 39-2378 and International Series Release No. 1208 (October 22, 1999). The Release was issued concurrently with the publication of another significant release (SEC Release 33-7760, 34-42055) adopting new rules, including Regulation M-A, regarding the regulation of takeovers and security holder communications.

2. SEC Release No. 33-7611, 34-40678 (November 13, 1998).

3. The methodology for determining the percentages of subject company securities held by investors resident in the United States for each of the new exemptions is discussed below under "Determination of U.S. Ownership."

- Second, the new "Tier II" exemption extends limited relief with respect to areas of frequent conflict between U.S. and foreign tender regulatory requirements in circumstances where U.S. holders own 40 percent or less but more than 10 percent of the class of securities of a foreign private issuer sought in a tender or exchange offer. This exemptive relief largely represents a codification of past SEC exemptive and interpretive positions. Apart from this relief, tender offers and exchange offers qualifying for the Tier II exemption will generally need to comply with U.S. requirements.

- Third, revised and renumbered Rule 14e-5 permits purchases of securities of a foreign private issuer outside of a pending Tier I tender offer or exchange offer both inside and outside the United States, subject to certain conditions. Previously, purchases of equity securities outside of a tender offer or exchange offer would generally have violated Rule 10b-13 under the Exchange Act the predecessor of Rule 14e-5.

- Fourth, new Rule 801 under the Securities Act of 1933 (the "Securities Act") exempts securities issued in rights offerings by foreign private issuers from the registration requirements of the Securities Act, subject to certain conditions, if U.S. holders own 10 percent or less of the class of equity securities that is the subject of the rights offering.

- Fifth, new Rule 802 under the Securities Act exempts securities issued in Tier I exchange offers from the registration requirements of the Securities Act and the qualification requirements of the Trust Indenture Act of 1939 (the "Trust Indenture Act"), subject to certain conditions. The exemption is available to both U.S. and foreign bidders.

Notwithstanding the new exemptions, the anti-fraud and anti-manipulation rules of the U.S. securities laws will continue to apply to all transactions with a U.S. nexis.

Each of the new exemptions is discussed in greater detail and analyzed below.

TIER I EXEMPTION

The Tier I exemption exempts tender offers and exchange offers from certain rules[4] under the Exchange Act regulating, among other things, the scope of required disclosure, timing of filings, minimum offer periods, withdrawal rights and proration. The Tier I exemption is available subject to satisfaction of the following conditions:

- U.S. holders own 10 percent or less of the class of securities which is the subject of the tender offer or exchange offer;

4. Rule 13e-3 (which regulates certain "going private transactions"), Rule 13e-4 (which regulates self-tender offers for equity securities which are registered under the Exchange Act), Regulation 14D (which regulates third-party tender offers for equity securities which are registered under the Exchange Act) and Rules 14e-1 and 14e-2 (which contain certain basic procedural requirements for tender offers) will not apply to offers qualifying for the Tier I exemption.

- the bidder submits to the SEC an English language translation of the offering materials under cover of Form CB, a new form, and files a consent to service of process on Form F-X if the transaction would otherwise have required SEC filings under Rule 13e-4 or Regulation 14D;

- U.S. holders are given the opportunity to participate in the offer on terms at least as favorable as those offered to any other holders, including price, type of consideration and choice among different alternatives being offered, duration, proration and withdrawal rights, subject to certain exceptions; and

- the bidder provides U.S. holders with offering materials in English on a basis comparable with other securityholders.

The Tier I exemption is available to U.S. and foreign bidders alike and is available for offers where the consideration consists, in whole or in part, of securities as well as for all cash tender offers. As discussed below, new Rule 802 exempts Tier I exchange offers from the registration requirements of the Securities Act. As a result of these exemptions from both Exchange Act and Securities Act requirements, Tier I exchange offers are now more competitive with cash offers for the same target company.

The SEC has also sought to achieve a level playing field in the case of competing offers by providing that if a second bidder commences a tender offer or an exchange offer during the pendency of another tender offer or exchange offer for same class of securities, the second bidder can rely upon the same exemption (Tier I, Tier II or Rule 802) as the prior offeror if all the conditions of the relevant exemption, other than the limitation on U.S. ownership, are satisfied by the second bidder. This provision will protect subsequent bidders launching new offers from being disadvantaged by the movement of securities into the United States following the commencement of prior offers.

In some circumstances, an initial bidder may seek a tactical advantage over subsequent bidders by *not* relying on the new exemptions if the initial bidder anticipates that post-commencement movements of the targeted securities would result in the Tier I, Tier II or Rule 802 exemptions becoming unavailable to subsequent bidders. This tactical advantage may arise, for example, in circumstances where the initial bidder takes advantage of a confidential pre-filing SEC review of a registration statement and commences its offer with an effective registration statement. Subsequent bidders might be faced with delays arising from the registration process if more than 10 percent of the target securities were held in the United States when they wished to launch their competing offers.

The Tier I exemption is conditioned upon bidders permitting U.S. security holders to participate in the offer on terms at least as favorable as those offered to other holders, subject to certain exceptions relevant to exchange offers. In the context of exchange offers, the SEC permits bidders to offer a cash alternative to U.S. holders. As adopted, U.S. holders may be offered only cash, even if non-U.S. holders are offered securities or a combination of cash and

securities, provided that the bidder has a reasonable basis to believe that the cash is substantially equivalent to the value of the securities and any cash or other consideration offered to non-U.S. holders. In order to ensure that U.S. holders receive substantially equivalent value for their securities, if the security offered outside the United States is not a "margin security"[5] within the meaning of Regulation T, the bidder must provide upon the request of the SEC or a U.S. holder, an opinion from an independent expert stating that the cash-only consideration is substantially equivalent to the securities and any cash offered outside the United States. If the security included in the offer outside the United States is a "margin security," the bidder must agree to provide the SEC and any requesting U.S. holder with closing prices and trading volumes for the offered security for each day in the six months preceding the announcement of the offer and each trading day thereafter.

The Tier I exemption also permits bidders to offer "loan notes" to non-U.S. security holders but not to U.S. holders. Bidders frequently offer a loan note alternative in bids for U.K. companies because such notes allow U.K. shareholders to defer recognition of income under U.K. tax rules. Bidders often prefer not to extend a loan note alternative to U.S. shareholders since it offers U.S. shareholder-taxpayers no U.S. tax advantage but may otherwise burden the bidder with registration requirements under the Securities Act. The Tier I exemption as adopted codifies prior exemptive relief by permitting a bidder to offer loan notes solely to non-U.S. holders in order to offer non-U.S. tender participants tax advantages not available in the United States, provided that these notes are neither listed on any organized securities market nor registered under the Securities Act.

The Tier I exemption also includes exceptions to the equal treatment condition in circumstances where U.S. state securities or "blue sky" laws make it difficult or impossible to offer securities to residents of particular states. If a bidder has determined to offer securities to all U.S. holders on the basis of the new Rule 802 exemption, the bidder may exclude U.S. holders residing in any state that does not provide an exemption from registration or qualification under that state's law. Similarly, if the bidder registers the offered securities under the Securities Act, the bidder may exclude U.S. holders residing in any state that refuses to register or qualify the offer and sale of securities in that state after a good faith effort by the bidder. In both cases, however, the bidder must offer the excluded holders cash instead of excluding them from the offer completely, if the bidder has offered cash-only consideration to holders in another state or in a jurisdiction outside the United States.

While the Tier I exemption simplifies the inclusion of U.S. investors in tender offers and exchange offers for securities of foreign private issuers where U.S. holders account for 10 percent or less of the subject securities, the exemption does not affect the continued application of U.S. anti-fraud and anti-manipulation laws to all tender offers and exchange offers having a

5. All stocks that appear on the Financial Times/Standard & Poor's Actuaries World Indices constitute "margin securities" for the purposes of Regulation T as well as the specific securities listed in such regulation.

U.S. nexis. Accordingly, while a bidder may not be separately required to observe the specific requirements of Rule 13e-3, Rule 13e-4, Regulation 14D, Rule 14e-1 and Rule 14e-2, to the extent that these rules are intended to prohibit particular activities which are regarded as fraudulent or manipulative, these rules will continue to provide important reference points in connection with the preparation of offering materials and the conduct of tender offers and exchange offers.

TIER II EXEMPTION

The Tier II exemption offers limited relief from the Exchange Act rules in connection with tender offers and exchange offers where U.S. holders own more than 10 percent but not more than 40 percent of the class of securities sought in the offer.[6] This exemption largely codifies past SEC exemptive and interpretive positions in areas of frequent conflict between U.S. and foreign regulatory requirements. The Tier II exemption:

- permits bidders to divide offers into two separate offers having the same terms:

  (i) a U.S. offer complying with the U.S. regulatory scheme and available to U.S. holders and (ii) a non-U.S. offer complying with the home jurisdiction rules which is unavailable to U.S. holders;

- allows requirements for prompt payment for, or return of, tendered securities to be determined in accordance with the requirements and practices of the target company's home jurisdiction;

- allows bidders to announce extensions of the offer in accordance with the practices of the home jurisdiction, rather than requiring any such announcement to be made before the commencement of trading on the next business day as required by the U.S. rules; and

- allows bidders to reduce or waive a minimum acceptance condition without extending withdrawal rights past the twentieth business day of a tender offer provided that the bidder

  — announces its intention to reduce or waive the minimum condition at least 5 business days in advance,

  — makes withdrawal rights available during 5-day period between the announcement and the reduction or waiver becoming effective and

6. As in the case of the Tier I exemption, if a bidder commences a tender offer or a business combination during the pendency of another tender offer or business combination for same class of securities, the second bidder can rely upon the same exemption as the prior offeror provided that all the conditions of the relevant exemption, other than the limitation on U.S. ownership, are satisfied by the second bidder.

— keeps the offer open for acceptances for at least 5 business days after the reduction or waiver becomes effective.

The SEC's recent adoption of Regulation M-A served to eliminate certain other areas of frequent conflict between U.S. and foreign rules. Regulation M-A eliminates the requirement for cash tender offers to commence within five business days of the announcement of the transaction, a requirement that often conflicted with longer periods permitted by foreign law. Regulation M-A also allows third-party bidders to provide for a "subsequent offer period," without withdrawal rights, similar to the offer structure commonly used in the U.K.

Because the Tier II exemption is designed to address circumstances in which shares held by U.S. holders represent a larger percentage of a target company's outstanding shares, the SEC has presumed (i) that there is less risk of such shareholders being excluded, and (ii) that there is greater need and justification for applying the relevant U.S. securities laws. Unlike offers eligible for the Tier I exemption, offers made subject to the Tier II exemption must therefore continue to be made pursuant to many of the requirements of U.S. tender offer laws, including the specific disclosure, filing and procedural requirements applicable to U.S. tender offers. In particular, the Tier II exemption does not provide relief from

- the requirement that an offer be open for at least 20 business days and be extended for a minimum amount of time in the event of certain changes in the offer,
- the specific disclosure requirements of Regulation 14D or the specific going-private disclosure and procedural requirements of Rule 13e-3 or
- the general anti-fraud and anti-manipulation rules.

The exemptions referred to above are subject to certain conditions. These conditions are similar to those which the SEC has required in granting previous exemptive relief, largely in the context of U.K. tender offers and the rules of the U.K. City Code. While these conditions have enabled many bids to proceed in compliance with local law and would be expected to be generally acceptable in the future, the SEC has also left open the possibility of continuing to grant specific ad-hoc relief on a case-by-case basis if the facts and circumstances require and justify additional relief.

RULE 14E-5: EXCHANGE ACT EXEMPTIONS FOR PURCHASES OF SECURITIES OUTSIDE OF A PENDING OFFER

U.S. rules, in particular Rule 10b-13, have historically prohibited bidders and persons affiliated with or acting for bidders, such as a dealer-managers, from purchasing, directly or indirectly, the securities that are subject to a tender offer other than pursuant to the offer. However, the laws in other jurisdictions have permitted bidders to purchase shares outside the offer, provided that the bidder provides consideration in the offer at least equal to the highest price paid for the subject securities outside the offer. Pursuant to the Release and the release

adopting Regulation M-A, the SEC has established a new limited exception for purchases outside of tender offers and exchange offers and has clarified and redesignated Rule 10b-13 as Rule 14e-5.

Rule 14e-5 permits purchases of subject securities outside the tender offer or exchange offer, inside or outside the United States, provided that:

- the tender offer or exchange offer qualifies as a Tier I offer;
- the U.S. offer document discloses prominently the possibility of purchases or arrangements to purchase the subject securities outside the offer as well as the manner in which disclosure of information regarding any such purchases will be made;
- the bidder discloses in the United States information about such purchases in a manner that is comparable to disclosure made in the target company's home jurisdiction; and
- the purchases comply with applicable tender offer laws in the target company's home jurisdiction.

Because of the greater U.S. interest in Tier II offers, the SEC has not extended the Rule 14e-5 exceptions to Tier II offers. Instead, the SEC has announced that in connection with offers not eligible for the Tier I exemption, the SEC will consider specific requests to permit purchase of target securities outside of the tender offer on a case-by-case basis in the light of relevant facts and circumstances.[7]

Rule 14e-5 also codifies certain relief which the SEC has previously granted to permit "connected exempt market makers" and "connected exempt principal traders", as defined by the U.K. City Code, to continue their U.K. market making activities during a cross-border offer that is subject to the City Code. Without such an exemption, when such market makers and traders are affiliated with a bidder's financial advisors, the U.S. rules would otherwise require them to withdraw from the market, with possible adverse consequences for the liquidity of the subject security. This exemption is available for both Tier I and Tier II offers, but is subject to certain disclosure and other requirements and conditions.

RULE 801 AND RULE 802: SECURITIES ACT EXEMPTIONS FOR RIGHTS OFFERINGS, EXCHANGE OFFERS AND BUSINESS COMBINATIONS

Rules 801 and 802 under the Securities Act provide exemptions from the registration requirements of the Securities Act for certain securities issued to U.S. holders in rights offerings,

7. In this context, we note that in the proposing release the SEC cited recent relief requested by this firm on behalf of its client Trinity Acquisition PLC in connection with its bid for Willis Corroon Group PLC. In that transaction, the bidder was granted relief from Rule 10b-13 even though 45.5 percent of the target's securities were held by U.S. holders.

exchange offers or business combinations. The exemptions from registration under Rule 801 and Rule 802 are available only if:

- the offeror in any rights offering relying on Rule 801, or the target company (including the issuer, in the case of an issuer offer) of any exchange offer or business combination relying on Rule 802, as the case may be, is a foreign private issuer;

- U.S. holders own 10 percent or less of the class of securities which is the subject of the offer;

- the terms and conditions of the offer are the same for U.S. and foreign securityholders, subject to the same U.S. state securities law exceptions applicable to Tier I offers; and

- in the case of rights offerings subject to Rule 801, (i) the securities offered are equity securities[8] of the same class as those held by offerees and are offered only for cash and only on a pro rata basis to existing holders and (ii) the rights granted to U.S. holders to subscribe for such equity securities are not transferable except outside the United States in accordance with Regulation S under the Securities Act.

The new exemptions restrict the transferability of the securities acquired in an exempt transaction if the securities to which they relate or for which they were exchanged were restricted. The general notes to the new rules indicate that securities acquired in a rights offering in reliance upon Rule 801 are "restricted securities" within the meaning of Rule 144 to the same extent and proportion that the securities held by the security holder as of the record date for the rights offering were restricted securities. Similarly, securities acquired in an exchange offer or business combination in reliance upon Rule 802 are "restricted securities" within the meaning of Rule 144 to the same extent and proportion that the securities tendered or exchanged by the security holder in that transaction were restricted securities. Consequently, if the securities that are the subject of the transaction made pursuant to Rule 801 or 802 are unrestricted, then securities acquired in the transaction will be unrestricted and will generally be freely tradable by non-affiliate securityholders immediately upon issuance.

Neither Rule 801 nor 802 requires the dissemination to U.S. holders of any specific information, but each Rule requires that any document, notice or other information that is provided to offerees be provided in English to U.S. offerees. If any information is made available outside of the United States by publishing it in a newspaper or similar publication, then a copy of the information must be published in the United States in a manner reasonably calculated to inform U.S. holders. Since any offering materials used in the U.S. will be subject to the anti-fraud provisions of Rule 10b-5, issuers will need to give careful consideration to the accuracy and completeness of such materials.

8. The term "equity securities" in the context of Rule 801 does not include convertible securities, warrants, rights or options.

Both Rules require that a legend be included in the offering document or notice stating that the offering is being conducted pursuant to home jurisdiction disclosure requirements, and that those requirements may differ from the U.S. disclosure requirements, including financial statement requirements. Under both Rules, the offeror is required to submit a notification on Form CB to the SEC that includes a copy of any document, notice or other information mailed to U.S. offerees. In addition, the offeror must appoint an agent for service of process in the United States by filing a Form F-X.

The Rule 802 exemption from registration is available to U.S. issuers, including U.S. public companies, even in circumstances in which Regulation S, the exemption for offshore offerings, would be unavailable for those U.S. issuers. As a result, U.S. companies should be able to compete more effectively with foreign bidders in exchange offers, and other business combinations involving stock, that are directed at foreign targets.

Rule 802 permits bidders to offer debt or equity securities in an exchange offer or business combination for the target's equity or debt securities. Although the issuance of debt securities in the U.S. ordinarily requires the qualification of an indenture under the Trust Indenture Act and the filing of a Form T-1, a new rule under the Trust Indenture Act exempts any debt security issued pursuant to Rule 802 from compliance with the relevant provisions of the Trust Indenture Act.

The exemptions provided by Rules 801 and 802 are non-exclusive. The notes accompanying the new rules indicate that securities issued in reliance upon the new rules will not be integrated with any other unregistered offerings of an issuer, even if the offerings occur concurrently.

The exemptions available under Rules 801 and 802 do not affect the anti-fraud or anti-manipulation provisions of the federal securities laws or provisions of state law relating to the offer and sale of securities. However, the civil liability provisions of the Securities Act that relate only to registered offerings will not apply to these transactions.

Exempt offerings under Rules 801 or 802 will not trigger the continuous reporting obligations of the Exchange Act or disqualify issuers from the exemption from such reporting requirements available under Rule 12g3-2(b) under the Exchange Act.

DETERMINATION OF U.S. OWNERSHIP

Determining the level of U.S. ownership of the subject or underlying securities is critical to an assessment of the availability of the Tier I and Tier II exemptions, as well as to the availability of the exemptions afforded by Rule 14e-5 and Rules 801 and 802. In each case, the availability of relief from the provisions of the Exchange Act or the Securities Act, as the case may be, depends in part on the percentage of the subject company's securities held by U.S. holders.

The determination of U.S. ownership of subject company securities for the purposes of the Tier I and Tier II exemptions, Rule 14e-5 and Rules 801 and 802 focuses primarily on beneficial, rather than record, ownership. The new exemptions require that the calculation of the percentage of outstanding securities held by U.S. holders be made as of the record date for a rights offering, or 30 days before the commencement of a tender offer, exchange offer or the solicitation for a business combination. In determining the amount of subject company securities outstanding, the offeror must include securities underlying American Depositary Shares, but must exclude other types of securities that are convertible or exchangeable into the securities that are the subject of the tender offer, such as warrants, options and convertible securities. In addition, securities that are held by persons who hold more than 10 percent of the subject securities, or that are held by the offeror in a tender offer, exchange offer or business combination are not considered outstanding subject company securities.

For the purposes of identifying subject company securities held by U.S. holders, the rules require that the offeror look through certain bank, broker-dealer and other nominees to determine the residence of the nominee's client accounts, as contemplated by Rule 12g3-2(a) under the Exchange Act. Offerors may limit their inquiries, however, to securities held of record

- in the United States,
- in the subject company's jurisdiction of incorporation or that of each participant in a business combination, in the case of a third party tender offer or exchange offer, or the issuer's jurisdiction of incorporation, in the case of issuer tender offers, issuer exchange offers and rights offerings, and
- in the jurisdiction that is the primary trading market for the subject securities.

If, after reasonable inquiry, the offeror is unable to obtain information about the amount of securities represented by accounts of customers resident in the United States, the offeror may assume that the customers are residents of the jurisdiction in which the nominee has its principal place of business. Finally, the rules require that the offeror count securities as owned by U.S. holders when publicly filed reports of beneficial ownership or information that is otherwise provided to the offeror indicates that the securities are held by U.S. residents.

The SEC has recognized that these rules would frequently be unworkable in the context of tender offers, exchange offers and business combinations which are not made on an agreed or friendly basis. Accordingly, the rules provide that, in a tender offer or exchange offer by a bidder other than an affiliate of the issuer of the subject securities, the issuer of the subject securities will be presumed to be a foreign private issuer and U.S. holders will be presumed to hold 10 percent or less (40 percent or less in the case of a Tier II offer) of such outstanding securities, unless:

- the tender offer or exchange offer is made pursuant to an agreement with the issuer of the subject securities;

- the aggregate trading volume of the subject class of securities on all national securities exchanges in the United States, on the Nasdaq market, or on the OTC market, as reported to the NASD, over the 12-calendar-month period ending 30 days before commencement of the offer, exceeds 10 percent (40 percent in the case of a Tier II offer) of the worldwide aggregate trading volume of that class of securities over the same period;

- the most recent annual report or annual information filed or submitted by the issuer of the subject securities with securities regulators of the home jurisdiction or with the SEC indicates that U.S. holders hold more than 10 percent (40 percent in the case of a Tier II offer) of the outstanding subject class of securities; or

- the bidder knows or has reason to know that the level of U.S. ownership exceeds 10 percent (40 percent in the case of a Tier II offer) of such securities.

These latter two provisions may cause some foreign issuers to consider publicizing their U.S. ownership levels (in annual reports or similar documents) as a defensive measure to prevent unwanted bidders from utilizing the exemptions.

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If you have any questions concerning the new exemptions or the Release, please contact Walt Looney, William Dougherty, Gregory Conway or Michael Wolfson of this firm's London office at +44-20-7422-4000, John Lobrano or Alan Klein of this firm's New York office at +1-212-455-2000, David Sneider of this firm's Tokyo office at +81-3-5562-8601, John Riley of this firm's Hong Kong Office at +852-2514-7600 or Alan Brenner of this firm's Singapore office at +65-430-5100.

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