Cross-Border Liability Management and U.S. Federal Securities Law

Exemptions from the U.S. Tender Offer Rules

Tender offers that are extended into the United States are subject to significant procedural and substantive requirements of the U.S. tender offer rules under the U.S. Securities Exchange Act of 1934 (the “Exchange Act”). These include a minimum offer period and prompt payment, among other requirements, as we discuss in detail in our note Cash Tender Offers for Non-Convertible Debt Securities. As a result, a non-U.S. issuer making a tender offer for its debt securities to U.S. holders will be required to structure the transaction to comply with limitations and requirements that are more restrictive than those that apply to offers conducted solely in its local market in Europe, Asia or elsewhere outside of the United States. However, consistent with U.S. Securities and Exchange Commission (“SEC”) policy to encourage the inclusion of U.S. holders in cross-border tender offers, exemptions from some of the requirements of the U.S. tender offer rules are available for certain tender offers for securities with limited U.S. beneficial ownership.

In this note, we provide an overview of the scope and the requirements of these exemptions. We also discuss current SEC interpretive guidance on measures to be taken to avoid U.S. jurisdiction altogether – an approach foreign issuers may choose to take where an exemption from the U.S. tender offer rules is not available or where inclusion of U.S. holders is not a priority.

Cross-Border Exemptions

The cross-border exemptions from the U.S. tender offer rules are structured as a two-tiered system based on the percentage of target securities beneficially held by U.S. residents ("U.S. holders").

**Tier I**

The “Tier I” exemption provides broad relief from the disclosure, filing and procedural requirements of the U.S. tender offer rules if the issuer of the target securities is (1) a foreign private issuer that (2) is not an investment company within the meaning of the U.S. Investment Company Act of 1940 (the “Investment Company Act”) other than a registered closed-end investment company and (3) 10% or less of the securities sought in the tender offer are beneficially held by U.S. holders.

The Tier I exemption requires that U.S. holders be allowed to participate in the tender offer on terms equally as favourable as those extended to non-U.S. holders. In addition, any informational documents provided to non-U.S. holders must also be provided to U.S. holders, in English, on a “comparable basis” to that provided to non-U.S. holders, and information published in the offeror’s home jurisdiction must be published in a manner “reasonably calculated” to inform U.S. holders of the offer.

Where an exchange offer is contemplated, a transaction meeting the Tier I requirements is generally also exempt from the registration requirements of the U.S. Securities Act of 1933 under Rule 802 thereunder, with similar requirements applying with respect to the provision of information to U.S. holders. The Rule 802 exemption is discussed in more detail in our note Debt Exchange Offers.

**Tier II**

The “Tier II” exemption provides more narrowly targeted relief from the U.S. tender offer rules designed to address certain common areas of conflict between the U.S. tender offer rules and the regulatory requirements of other jurisdictions. This exemption is available if (1) the offeror is a foreign private issuer that (2) is not an investment company within the meaning of the Investment Company Act of 1940 other than a registered closed-end investment company and (3) U.S. holders beneficially own more than 10% but no more than 40% of the target security.

Tier II offers enjoy exemptive relief from the prompt payment and notice of extension requirements of Rule 14e-1 and limited relief

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A foreign (non-U.S. incorporated) company will qualify as a foreign private issuer if 50% or less of its outstanding voting securities are held by U.S. residents or if more than 50% of its outstanding voting securities are held by U.S. residents and none of the following three circumstances applies: the majority of its executive officers or directors are U.S. citizens or 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. A company that is incorporated in a state, territory or possession of the United States can never qualify as a foreign private issuer.
from the prohibition on the purchase of target equity securities by the issuer and certain other persons outside of the tender offer during the offer period under Rule 14e-5. The offer may instead be conducted pursuant to the corresponding requirements of the offeror’s foreign home jurisdiction. Tier II offers are not, however, exempt from the broader regime governing tender offers including the offer period requirement of 20 U.S. business days.2

Where U.S. holders beneficially own more than 40% of the relevant target securities, all requirements of the U.S. tender offer regime apply to the transaction. Moreover, neither of the cross-border exemptions provides relief from the anti-fraud and anti-manipulation rules of the U.S. federal securities laws.

Determining U.S. Beneficial Ownership – Look-Through Analysis
To determine eligibility for relief under either exemption, the offeror must “look through” the record ownership of banks, brokers, dealers and other nominees resident in specified jurisdictions to identify interests beneficially owned by U.S. holders. These jurisdictions are the United States, the issuer’s jurisdiction of incorporation, the primary trading market of the target security and, if the debt securities are guaranteed, the home jurisdiction of each guarantor. If after “reasonable inquiry” the offeror is unable to obtain information about a nominee’s customer accounts, the offeror may assume that the customers are residents of the jurisdiction in which the nominee has its principal place of business.

The eligibility determination must generally be made as of a date no more than 60 days before, and no more than 30 days after, the public announcement of the transaction. If the offeror is unable to conduct the look-through analysis within this 90-day period – for example, where practices in the relevant home jurisdiction do not allow it – the rules permit the calculation of eligibility to be made as of the most recent practical date before public announcement, but in no event earlier than 120 days before announcement. The look-through analysis is the primary method to determine eligibility for Tier I or Tier II exemptive relief. However, in certain limited circumstances in which a look-through exercise cannot be conducted (e.g., when the securities are held in bearer form or nominees are prohibited by law from disclosing information about beneficial owners), the SEC permits the use of an alternate test based on trading volume of the subject securities in the United States.3,4

Where debt securities are held in registered form through common clearing systems, such as Euroclear, Clearstream or The Depository Trust Company (“DTC”), the look-through analysis can be completed relatively quickly (generally within two to three weeks) and cost-effectively by a specialist firm.3 For securities issued outside the United States in bearer form – an approach that remains common among non-U.S. issuers, particularly in Europe – identification of beneficial holders is potentially more problematic.

Avoiding U.S. Jurisdiction
The SEC encourages offerors in cross-border tender offers to take advantage of the above exemptions to permit U.S. holders to participate in such transactions. However, a non-U.S. offeror making a tender offer for its securities can avoid the application of the U.S. tender offer rules altogether if the offer is conducted outside the United States, U.S. jurisdictional means are not used and U.S.-based holders are thereby excluded from the offer.

The Exchange Act does not prescribe a method for avoiding U.S. jurisdictional means, and certain such attempts have been the subject of litigation. However, the staff of the SEC has indicated that legends and disclaimers to the effect that an offer is not being made into the United States and that offer materials may not be distributed there will alone not be sufficient. The offeror must implement adequate measures to safeguard against purchases from and, in the case of exchange offers, sales of securities to, holders in the United States.

For example, the offer document should not be sent into the United States and forms of acceptance should not be received from the United States. In addition, the offeror should consider the following safeguards:

- > stating in the offering materials that nominees, custodians and other intermediaries should not forward the materials to persons in the United States;
- > not permitting participation in the offer by anyone in the United States, and not acknowledging any acceptance where the form of acceptance indicates that it has been sent from the United States;
- > requiring representations from tendering holders that they are not located or resident in the United States and are not tendering securities on behalf of such persons;
- > not soliciting interest from holders in the United States or providing information about the transaction into the United States, even on a reverse-enquiry basis; and
- > implementing restrictions on publicity, including not having any road shows in the United States and only distributing press releases outside the United States (with appropriate legends).

Practical Application of the Exemptions
The SEC promulgated the Tier I and Tier II exemptions to encourage foreign private issuers to extend cross-border tender and exchange offers to U.S. holders. Despite this policy goal, market participants infrequently rely on these exemptions.

As discussed above, the scope of Tier II exemptive relief is limited. As a result, in the absence of unusual factors that make the U.S. settlement cycle difficult to comply with, the added time and expense of performing a look-through analysis generally may not be worth the benefits that could be obtained.

Tier I relief is much broader and potentially useful in affording significant additional flexibility in structuring the offer, including in circumstances where maximising tender offer participation is important for commercial reasons or where extending the offer to all holders is a requirement under local law or the terms of the target securities. Nevertheless, the Tier I exemption also remains underutilised in practice, as issuers with few U.S. holders can generally achieve the commercial goals of a tender offer even if these holders are excluded.

Other notes in our Cross-Border Liability Management and U.S. Federal Securities Law series can be found here.

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2 The SEC has also granted no-action relief from the 20-day minimum offer period requirement of Rule 14a-1(a) where it conflicts with local law requirements. See, e.g., Patni Computer Systems Limited, SEC No-Action Letter (9 February 2011) and Satyam Computer Services Ltd., SEC No-Action Letter (28 April 2009), where relief was granted on the basis that the Indian Takeover Code required a 20-calendar day tender offer period and provided for a seven-business day extension following an announcement of a change in material terms of the offer; and SoFiFin, SEC No-Action Letter (15 April 2009), where relief was granted on the basis that the offer was conducted in 11 business days in accordance with the requirements of special legislation intended to facilitate the restructuring of a systemically important mortgage lender in Germany.

3 The alternative test is satisfied where (1) in the 12-month period ending no more than 60 days before announcement the average daily trading volume (“ADTV”) of the target securities in the United States is no more than 10% (Tier I) or 40% (Tier II) of their ADTV worldwide; (2) information suggesting otherwise is not available in the issuer’s public filings; and (3) the offeror does not know, or have reason to know, that U.S. beneficial ownership exceeds the applicable limit.

4 The SEC has clarified that time- and expense-related considerations and concerns about the completeness and accuracy of the information obtained alone will not support a finding that an offeror is unable to conduct the look-through analysis.

5 On completion of the survey, the firm conducting it will generally provide the offeror with a letter describing the methodology employed and the outcome of the analysis. The letter can serve as a useful factual record of the look-through analysis.
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