International Lawyer

Volume 21 | Number 3 | Article 10

1987

EEC Law and Other Problems in Applying the SEC Proposal on Multinational Offerings to the U.K.

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The term "Internationalization of the Securities Markets" can be understood in two ways: It can mean the internationalization of the "primary" markets, i.e., the facilitation of initial transborder securities offerings, or it can mean the internationalization of secondary trading, i.e., the listing of securities on stock exchanges in more than one country.[1] This distinction can readily be derived from the separation of the American law of securities regulations into two statutes, the Securities Act of 1933[2] and the Securities Exchange Act of 1934.[3]

While it has historical reasons in the United States the distinction between issuance and trading does not necessarily make sense. Under present EEC law securities issued and distributed to the public become subject to regulation only if they are to be traded on the stock exchange.[4]

This article focuses on the efforts of the Securities and Exchange Commission (SEC) to facilitate multinational securities offerings as envisioned by SEC Release No. 33-6568.[5] In this release the SEC is concerned with

*Referendar iur., University of Frankfurt, 1983; LL.M., University of Illinois, 1986. The author wishes to thank Professor George T. Frampton of the University of Illinois College of Law for his guidance and support and the German Academic Exchange Service (DAAD) for the financial support of my stay at the University of Illinois.

†The Editorial Reviewer for this article is Werner F. Ebke.

1. *See* Pozen, *Disclosure and Trading in an International Securities Market*, 15 INT'L LAW. 84 (1981).

2. 15 U.S.C. §§ 77a-77aa (1982).

3. 15 U.S.C. §§ 78a-78kk (1982).

4. *Council Directive of 17 March 1980 (EEC) No. 80/390*, 23 O.J. EUR. COMM. (No. L 100) art. 1, at 1 (1980) [hereinafter *Prospectus Directive*]. A new draft directive, however, will cover unlisted securities as well. *See* 23 O.J. EUR. COMM. (No. C 355) at 39 (1980).

5. Exchange Act Release No. 33-6568, 17 Sec. Reg. & L. Rep. (BNA) 434, 50 Fed. Reg. 9281 (1985).

the problems of offerings made in more than one country at more or less the same time. The SEC acknowledges that global markets for initial offerings are evolving[6] by reason of the greater need, especially for institutional investors, to diversify their portfolios and to increase the return on their investments.[7] In 1985, although the American stock market showed tremendous percentage increases in stock prices, the German stock market showed even greater gains.

American investors use various methods of acquisition. Institutional investors frequently buy directly on the foreign stock market via an American or foreign brokerage house. Since they usually buy large blocks of securities, their transaction costs are comparably low.[8] On the other hand, small investors will often buy foreign securities by purchasing American Depository Receipts (ADRs).[9] The greatest amount of foreign securities are traded in the ADR market.[10]

A number of foreign securities are, however, traded directly in the U.S. market.[11] Increased offering directly to the American investor in the U.S. market will facilitate access for the foreign issuer and reduce transaction costs to the investor.[12] The SEC's efforts to facilitate access to U.S. capital markets can arguably be seen as difficult to reconcile with the SEC's duty to protect investors. Several arguments, however, favor allowing foreign issuers access under less stringent conditions than apply to domestic issuers. First, compliance with U.S. disclosure standards may involve a special hardship for the foreigner, for example, with respect to accounting standards.[13] In addition, securities laws in general hamper the free international flow of capital, thereby making it more difficult for foreign issuers to reach U.S. investors.[14]

One may question whether the SEC should have the responsibility of opening new (and perhaps risky) investment opportunities for American investors by facilitating the access of foreign issuers to the U.S. capital market. It can also be argued, however, that, given the increased tendency of the American investors to invest abroad, the best way to protect them

6. *See generally* Thomas, *The Internationalization of the Securities Markets: An Empirical Analysis*, 50 Geo. Wash. L. Rev. 155 (1982).

7. *Id.* at 163; Merloe, *Internationalization of Securities Markets: A Critical Survey of U.S. and EEC Disclosure Requirements*, 8 J. Bus. & Cap. Mkt. L. 249, 251 (1986).

8. Thomas, *supra* note 6, at 167.

9. *Id.* at 169 n.53.

10. *See* Royston, *The Regulation of American Depository Receipts: Americanization of the International Capital Markets*, 10 N.C.J. Int'l L. & Com. Reg. 87, 106 (1985).

11. *See* Pozen, *International Securities Markets: Comparative Disclosure Requirements*, 3 J. Comp. Corp. L. & Sec. Reg. 392, 422 (1981).

12. *See* Thomas, *supra* note 6, at 170.

13. *Id.* at 158.

14. *Id.* at 168.

is to have the transaction occur on an American instead of a foreign exchange. The SEC can police the foreign issuer most effectively if the issuer's shares are traded here,[15] even though recent tendencies abroad, for example, in the EEC, show more rigid disclosure requirements as well.

In its concern for multinational offerings,[16] the SEC focuses basically on a three-country mutual offering facilitation to include the U.S., Canada, and the U.K.,[17] having in mind some recent simultaneous offerings of U.K. and Canadian securities in the U.S. The release emphasizes the similarity of the regulatory approaches in those three countries. Of the European countries, the U.K. is presently the only one that has implemented into national law EEC harmonization legislation with regard to securities regulation.[18] Most authors emphasize the influence of the EEC Prospectus Directive on recent developments of U.S. disclosure rules for foreign issuers.[19] In other words, the inclusion of the U.K. in a multinational offering facilitation effort will be a paradigm for the opening of the U.S. capital market to the European issuer and a litmus test for the similarity of disclosure requirements in a transatlantic securities market.

Two considerations seem to facilitate a mutual recognition of prospectuses with regard to the U.K. First, the lack of a language barrier. Other European issuers who try to gain easy access to the North American securities market would have to translate the material, even if disclosure requirements in Europe and North America were in perfect harmony. Secondly, U.K. issuers have more often crossed the Atlantic with initial offerings and therefore have more experience in coping with the U.S. securities laws. U.K. issuers might be less frightened by the liability provisions in the U.S. The SEC Release emphasizes the similarities between the U.S. and the U.K. disclosure requirements,[20] but fails to focus on the recent implementation of three EEC directives that have substantially modified U.K. law.

This article reviews similarities and differences between U.S. and U.K. law with special emphasis on the EEC harmonization effort. Eventually the SEC proposal contained in SEC Release 33-6568 might be modified

15. *Id.* at 167-68.
16. 17 Sec. Reg. & L. Rep., *supra* note 5, at 435.
17. *Id.* at 434.
18. *See infra* text accompanying notes 114-31.
19. *See* Merloe, *supra* note 7, at 255. Pierce, *The Regulation of the Issuance and Trading of Securities in the U.S. and the E.E.C.: A Comparison,* 3 J. COMP. CORP. L. & SEC. REG. 129, 133 (1981); Thomas, *supra* note 6, at 168; Note, *Foreign Securities: Integration and Disclosure under the Securities and Exchange Acts,* 58 NOTRE DAME L. REV. 911, 919 (1983).
20. 17 Sec. Reg. & L. Rep., *supra* note 5, at 435-36.

to include offerings by other EEC issuers as well. The National Association of Securities Dealers suggested this idea in its comment on the SEC Release.[21] Therefore this article does not focus exclusively on the feasibility of harmonizing U.S. and U.K. disclosure requirements but also considers the EEC securities law in general.

The SEC approach is to look at the present state of the disclosure requirements in the U.K. and Canada and to compare them to U.S. law. The SEC envisions a joint harmonizing effort either by reciprocal recognition of prospectuses or the creation of a common prospectus. Either of those prospectuses would have to conform to a maximum extent with the securities laws of all three countries. In addition, a multinational offering involves timing and liability problems that require a focus on the different administrative procedures and the liability provisions.

Finally, a harmonization and facilitation effort across the Atlantic will be feasible only if the countries are allowed discretionary room to modify the present disclosure requirements. Administrative regulations are much easier to modify than statutory provisions. For example, the SEC can rather easily create a new registration form with less rigid disclosure requirements. The minimum statutory disclosure requirements are contained in Schedule A of the 1933 Act. These minimum requirements give the SEC a broad range of discretion with respect to details. Such ease of modification is not the case under EEC law. The contents of the prospectus is predefined by the EEC directive and is not subject to the discretion of the competent administrative authorities or even the national legislatures.

In short, any facilitation effort must start by establishing the largest common denominator for disclosure. Once this core is found, it remains to be seen how the remaining barriers can be removed, that is, how to guarantee indispensable minimum disclosure. Since the SEC envisions a mutual facilitation, another important inquiry is whether a U.S. prospectus would satisfy EEC disclosure standards. In that regard it should be emphasized again that the U.K. is not free to grant exemptions from EEC disclosure requirements, since the Prospectus Directive sets forth minimum standards in the EEC that cannot be undercut. This limitation is acknowledged by the London Stock Exchange.[22]

This article, then, encompasses a comparison of U.S. and U.K. disclosure requirements with emphasis on the indispensable minimum U.S. and EEC standards of disclosure in order to determine the feasibility of

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21. *See* Summary of Comments on Concept Release Facilitation of Multinational Securities Offerings by the SEC Division of Corporation Finance at 14, SEC Release No. 33-6568, File No. S 7-9-85 (Jan. 10, 1986) [hereinafter Summary of Comments] (copy on file with the author).

22. *Id.* at 15.

the proposals set forth in SEC Release 33-6568. Before examining the release in more detail, the present state of disclosure requirements for foreign issuers for initial distribution under the new integrated disclosure system in the U.S. are summarized.

I. The Present Status of Foreign Issuers in the U.S.

A. Registration under the 1933 Act

If a foreign issuer wants to offer securities in the U.S. by the "jurisdictional means," it must, as a general rule, comply with the registration requirement of section 5 of the 1933 Securities Act,[23] except, of course, if it qualifies for one of the small offering or private offering exemptions as contained in sections 3(b) and 4(2) of the 1933 Act and in Regulations A and D.[24] Otherwise, the issuer can avoid application of the 1933 Act only if the original primary distribution took place outside of the U.S. and all offered securities have come to rest abroad.[25] If the securities are thereafter injected into the U.S. secondary trading market, the issuer will be subject to SEC action only if it actively encourages trading.[26]

1. *Forms F-1, F-2, F-3*

The SEC has eased disclosure requirements for foreign issuers by introducing the "F-series" forms F-1, F-2, and F-3.[27] These forms are part of the new integrated disclosure system.[28] They consist of two parts. Part I is completely identical to the "S-series" forms for initial distribution of domestic securities; the registrant has to furnish the "500-series" items of Regulation S-K and Item 202 of Regulation S-K.[29]

Under Item 501 the issuer has to furnish a specific forepart and front cover page of the prospectus. Item 502 defines the contents of the inside front and outside back cover pages. Item 503 requires summary information, and the description of risk factors and earnings ratios. In Item 504 the issuer has to explain the use of the proceeds. Item 505 requires an explanation of the computation of the offering price in some cases.

23. *See* R. Jennings & H. Marsh, Securities Regulation Cases and Materials 1304 (5th ed. 1982).
24. Regulation A, 17 C.F.R. §§ 230.251-.264 (1986); Regulation D, 17 C.F.R. §§ 230.501-.506 (1986).
25. *See* Note, *supra* note 19, at 916.
26. *Id.* at 916-17.
27. Form F-1, 47 Fed. Reg. 54,771 (1982); Form F-2, 47 Fed. Reg. 54,773 (1982); Form F-3, 47 Fed. Reg. 54,776 (1982); Convenient Reference: 2 Donelly, SEC Handbook 11-2-3 (1985).
28. *See generally* Bloomenthal, *The Integrated Disclosure System for Foreign Issuers*, 5 Sec. & Fed. Corp. L. Rep. (Clark Boardman) (Feb. 1983).
29. 17 C.F.R. §§ 229.10-.800 (1986).

Under Item 506 the dilution of equity resulting from the sale of stock by existing shareholders has to be disclosed. These selling shareholders have to be named under Item 507. The remaining items require a description of the plan of distribution (Item 508), a disclosure of the interest of named experts and counsel (Item 509), a statement on the SEC's negative view with respect to indemnification of officers for possible liabilities under the securities acts (Item 510), and a description of the costs of the issuance and distribution (Item 511).

Forms F-1, F-2, and F-3 are patterned after the forms for domestic issuers S-1, S-2, and S-3. These domestic forms create an integrated disclosure system, which allows the incorporation by reference of information filed under the 1934 Exchange Act. The idea behind the integrated disclosure system is to avoid the filing of information that is already in the hands of the SEC. In other words, the longer an issuer has been a reporting company under the 1934 Exchange Act, the more information can be incorporated by reference to these reports. This same idea has been implemented for foreign issuers as well.

In part II of Form F-1 the issuer has to give the information contained in the basic registration form for foreign issuers under the 1934 Exchange Act, Form 20-F.[30] Under Form F-1 all information under Form 20-F has to be given, whereas under Forms F-2 and F-3, this information can be incorporated by reference.

F-1 is the basic registration form that has to be used, unless the issuer qualifies for either Form F-2 or F-3. The registrant can use Form F-2 if he meets either of the following conditions: (1) The issuer is a reporting company under section 12 or 15(d) of the 1934 Exchange Act and has been filing all the required forms for the last thirty-six months,[31] or (2) the registrant is a "world class" issuer and has filed at least one Form 20-F.[32] An issuer is considered to be "world class" if the aggregate market value of its stock held by nonaffiliates ("float") exceeds $300 million. A registrant who qualifies for Form F-2 can incorporate its latest 20-F by reference and simply furnish an update. Under Form F-2 a copy of the latest 20-F has to be filed as an exhibit.[33]

A registrant qualifies for F-3 if it is a "world class" issuer and has been reporting under sections 12 or 15(d) of the 1934 Exchange Act for at least 36 months.[34] A non-"world class" issuer that has been a reporting company for at least thirty-six months can use Form F-3 for "investment

30. 17 C.F.R. §§ 249.220(f) (1986) (discussed *infra* text accompanying notes 55-62).
31. *See supra* note 27, Form F-2, General Instructions (B)(1), at 54,773.
32. *Id.* General Instructions (B)(2), at 54,774.
33. *Id.* Items 11 and 12, at 54,774.
34. *See supra* note 27, Form F-3, General Instructions (A)(2) and (A)(4), at 54,778.

grade nonconvertible debt."[35] Form F-3 is almost identical to Form F-2, i.e., the issuer can incorporate the latest 20-F and only has to update the information contained therein. Under F-3 however, no copy needs to be included in the filing.

Under Forms F-2 and F-3 the financial information in the latest 20-F must be conformed to Item 18, i.e., to U.S. GAAP and Regulation S-X.[36] The lesser financial disclosure standards, as contained in Item 17 of Form 10-F, may be used only for the issue of rights to existing shareholders in specific cases (provided that one such Form 20-F has been filed). If these conditions have been met, Form F-2 or F-3 may be used for rights offerings.[37] In an offering of investment grade nonconvertible debt securities on Form F-3, it is also sufficient that the latest 20-F contain Item 17 financial information, instead of the stricter standards contained in Item 18.[38]

The Appendix Table I clarifies this rather confusing scheme and shows under what circumstances the different forms may be used.[39]

2. *American Depository Receipts—Form F-6*

The registration of American Depository Receipts (ADRs) is by comparison much easier than the registration of foreign securities offered directly to the public. ADRs represent foreign securities held by a U.S. bank or trust company (depository).[40] One ADR represents one or more securities. ADRs are of course securities themselves and are subject to the registration requirements of the 1933 Act.[41] As long as the issuer of the underlying foreign securities does not actively encourage trading, the SEC will not enforce the securities laws against it (the so-called "voluntarism" principle).[42] The foreign issuer is not deemed to be the issuer of the ADRs.[43] The depository provides the service functions; it collects the interest or dividends and converts them into U.S. currency.[44] The issue of the ADRs is usually undertaken by an investment bank,[45] which

35. *Id.*, General Instructions (B)(2) and (A)(4), at 54,778.

36. *See supra* note 27, Form F-2, General Instructions (D) at 54,774; Form F-3, General Instructions (B)(1), at 54,778. (Item 18 in Form 20-F is discussed *infra* text accompanying notes 56-61.

37. *See supra* note 27, Form F-2, General Instructions (E), at 54,774.

38. *See supra* note 27, Form F-3, General Instructions (B)(2), at 54,778.

39. *See also* Merloe, *supra* note 7, at 262.

40. *See generally* Royston, *supra* note 10, at 87.

41. *Id.* at 88.

42. *Id.* at 88-89. These ADRs are called "unsponsored"; *see* Thomas, *supra* note 6, at 69 n.53.

43. *See* Royston, *supra* note 10, at 96.

44. *See* Note, *supra* note 19, at 912 n.5.

45. *See* Royston, *supra* note 10, at 97.

negotiates the depository agreement with the depository. The terms of this agreement generally appear on the ADR certificate itself.[46]

Since most of the ADRs provide that the underlying security may be withdrawn by the holder of the ADR, difficult problems with regard to the 1933 Act may arise.[47] The depository may be viewed as an underwriter, if the underlying security is withdrawn. Also an open question is whether the security holder who withdraws may sell the foreign security without restriction under section 4 of the 1933 Act.[48]

The issuer of the ADR, that is the investment bank, has to file a Form F-6. Prerequisite to use Form F-6 is registration of the underlying foreign securities or exemption of the securities from registration under the 1933 Act.[49] For example, if the foreign security was acquired in a private transaction, no registration is necessary under section 4(2) of the 1933 Act. In addition, the issuer of the underlying securities must be either a reporting company or a company exempt from the reporting requirements under SEC rule 12g3-2. Alternatively, the issuer may register concurrently by filing a Form 20-F.[50] In addition, registration on Form F-6 is possible only if the underlying securities may be withdrawn by the ADR holder.

If those requirements are met, registration of the ADRs on Form F-6 is fairly simple. The information of Item 202(f) of Regulation S-K has to be filed, plus a statement that information about the issuer of the underlying security is available at the offices of the SEC.[51] The prospectus can consist of a copy of the ADR certificate itself.[52] In addition the only documents to be filed are the depository agreement and some minor exhibits.[53] In sum, registration is fairly convenient. Note, however, that Form F-6 cannot be used to distribute the underlying securities to the public[54] and that the foreign issuer must be registered under the 1934 Exchange Act or be exempt from registration.

B. Form 20-F

Under the integrated disclosure system, the core of any issue of a security on the F-series forms is the information to be filed on Form 20-F.

46. *Id.* at 97.

47. *Id.* at 104-06 (the underlying security must be withdrawable if the ADRs are to be registered on Form F-6).

48. *See* Royston, *supra* note 10, at 104-06.

49. *See* 2 Fed. Sec. L. Rep. (CCH) §§ 7001-7005 (Mar. 18, 1983); Form F-6, General Instructions (I)(A)(2).

50. *Id.* General Instructions (I)(A)(3).

51. *Id.* Part I, Items 1 and 2.

52. *Id.* General Instructions III.B.

53. *Id.* Part II, Item 3.

54. *See* Royston, *supra* note 10, at 91.

The best way to approach this form is to review briefly the differences and similarities between the disclosure for domestic issuers on Form 10-K and the more lenient requirements under Form 20-F.[55] Like a domestic issuer, the foreign registrant has to furnish Management's Discussion and Analysis (Item 9), Selected Financial Data (Item 8), Legal Proceedings (Item 3), Directors and Executive Officers (Item 10), and Description of Properties (Item 2). Special provisions apply to oil and gas properties that will not be discussed here. The issuer must in addition furnish special information that takes into account the special problems of offerings of foreign securities: information about the currency exchange rate and restrictions in transborder capital flow (Item 6) and Taxation (Item 7).

The disclosure requirements are less strict in the following areas: the description of business is less extensive (Item 1); the description of research and development, new products, and services is less exhaustive. The most important relaxation is in the area of "segmented" reporting: the breakdown of sales and profits into the different fields of activity and geographical markets is less stringent. Segmented reporting is information that foreign issuers are reluctant to publish.[56]

The other area of major concession toward the needs of the foreign issuer is that of management remuneration (Item 11). The disclosure of an aggregate amount is sufficient. The individual salaries have to be given only if they are disclosed to the issuer's shareholders or if they are otherwise made public. The same concession has been made concerning the management's ownership of the registrant's shares. The aggregate amount is sufficient disclosure unless the individual holdings are published elsewhere. The same is true for options held by the management.

Another relaxation has been implemented with respect to certain transactions between the management and the issuer and/or its subsidiaries. These transactions have to be disclosed only to the extent that this information is made public at the issuer's domicile (Item 13). Even if the information has to be disclosed, the disclosure is less detailed than for domestic issuers.

One of the major concessions (if not the most important) has been achieved in the area of financial information. The foreign issuer can furnish financial statements according to the GAAP of its home country, if the divergences between these standards and U.S. generally accepted accounting principles (GAAP) are explained (Items 17 and 18). In other words, the financial statements need to be reconciled quantitatively. The issuer is given a choice between Items 17 and 18. The only difference

55. *See generally* Bloomenthal, *supra* note 28, at 10-16; Form 20-F, 17 C.F.R. § 249.220(f) (1982).

56. *See* Pozen, *supra* note 1, at 85.

between Items 17 and 18 is that in Item 18, with exception of the balance sheets, the financial information must conform to U.S. GAAP and Regulation S-X.[57] This requirement includes segmented reporting. Under Item 18, therefore, not only the "measurement principles," but also the "disclosure principles" must be reconciled.[58] To state it differently, Item 18 takes away the concession made in Item 1 for most practical purposes. In order to be of any use to the foreign issuer, Form 20-F has to comply with Item 18, since compliance with this item in the latest Form 20-F is a prerequisite for almost all offerings registered on Forms F-2 or F-3.[59] This can readily be derived from Table 1.

The only case where Item 17 can be used is for the offering of investment grade nonconvertible debt by a company that has reported for at least thirty-six months under the 1934 Exchange Act. Even a "world class" issuer has to furnish the increased financial disclosure demanded by Item 18 for an ordinary securities offering for cash.[60] The only case where this hurdle does not exist are Eurobond issues, which are placed mostly privately with institutional investors.[61] However in the future, it is possible that the SEC will grant waivers.[62]

To evaluate the burden imposed by the present U.S. disclosure system, one has to compare these requirements with the present state of disclosure under foreign law. This comparison is developed in section V below.

II. The SEC Proposal for Multinational Offerings

The SEC Release 33-6568 is less a proposal than an invitation for comment on how to deal with the problem of multinational offerings in the future. The SEC briefly outlines two basic concepts, but does not propose any detailed regulatory schemes. The SEC is concerned with some recent simultaneous offerings. For example the Reuter plc. offering grew out of the assumption that one single securities market alone could not possibly have absorbed the entire issue.[63] Another reason for multinational offer-

57. *See* Form 20-F, Item 18(3), 47 Fed. Reg. 54,781, 54,788 (1982).

58. *See* Summary of Comments, *supra* note 21, at 18 n.11.

59. *See supra* note 27, Form F-2, General Instructions (D), at 54,774; Form F-3, General Instructions (B)(1) and (B)(3) at 54,778.

60. For a critique of disclosure demands, see Merloe, *supra* note 7, at 263; Note *supra* note 19, at 923. *But see* Karmel, *The SEC Goes International,* 193 N.Y.L.J., June 20, 1985, at 4, col. 2 (expressing the opposite view).

61. *See* Note, *supra* note 19, at 923.

62. *See* Thomas, *Increased Access to U.S. Capital Markets: A Brief Look at the SEC's New Integrated Disclosure Rules for Foreign Issuers,* 5 J. COMP. BUS. & CAP. MARKET L. 129, 132 (1983).

63. *See* Letter of the Section of Corporate, Banking and Business Law of the ABA, Appendix A at 4-5 (July 15, 1985) (response on the SEC's request for comment) [hereinafter ABA-Letter] (copy on file with the author).

ings is that trading a share on more than one national exchange enhances its value.[64] In the release the SEC correctly points out that prospectus uniformity alone is no solution. Divergences in the registration procedure and different liability provisions prove to be as cumbersome as different disclosure requirements.[65]

A. Reciprocity versus Commonality

The two different approaches in easing the disclosure requirements proposed by the SEC are the reciprocity approach and the common prospectus approach. Under the reciprocity approach, the three countries would agree to accept mutually the prospectuses filed in the home jurisdiction of the issuer under the condition that they meet a minimum standard agreed upon in advance. Review would be limited to the authorities in the home jurisdiction. The common prospectus approach would envision a single prospectus format agreed upon by the three countries that would of course lead to completely uniform disclosure standards. The liability provisions would remain unchanged under both approaches.[66]

The SEC is aware that the latter approach is much more unrealistic, since the three countries would have to agree on a common disclosure standard.[67] The SEC notes the following advantages for the reciprocity approach: it is simpler to implement, and is less costly and time consuming to achieve.[68] In the SEC's view the disadvantage of the reciprocity approach is that the participating countries might perhaps give up further efforts to harmonize disclosure and that the result would probably be less disclosure than under a common prospectus approach.[69] To the SEC the common prospectus approach has the advantage of creating a greater harmonization.[70]

The common prospectus approach would, however, not necessarily offer the same high disclosure standards now present in U.S. law. To achieve a common prospectus the U.S. would have to make compromises with respect to the minimum information. A disadvantage for the common prospectus seen by the SEC is the probably higher transaction cost for the foreign issuer resulting from a multiple review under the common prospectus approach.[71] However, it seems that under a reciprocity sys-

64. *Id.* at 15.
65. 17 Sec. Reg. & L. Rep. *supra* note 5, at 435-36.
66. *Id.* at 436.
67. *Id.*
68. *Id.* at 437.
69. *Id.*
70. *Id.*
71. *Id.*

tem, too, the issuer cannot be completely relieved from multiple filings, and under a modified reciprocity approach as proposed in the ABA-Letter discussed below, some limited form of review in the host country will be unavoidable. In addition, conceptually, there is no reason why a common prospectus should be reviewed by more than one authority.

B. The Request for Comment

In order to evaluate further the different options for dealing with the recurring problems in this area, the SEC requested comments from the securities lawyers' community. In addition, the SEC asked seventeen specific questions.[72] In total, the SEC received seventy responses, and fifty of fifty-seven responses that expressed a preference favored the reciprocity approach.[73]

The Section of Corporation, Banking and Business Law of the ABA wrote a lengthy comment.[74] The ABA, as well as most of the other proponents of a reciprocity approach, proposes a "modified" reciprocity approach, that is that a foreign prospectus be supplemented by additional disclosure of indispensable information.[75] Other commentators, including the London Stock Exchange, favor a per se reciprocity, suggesting that at present, the U.K. and Canadian prospectuses satisfy U.S. disclosure standards.[76] The ABA mentions that its proposal is in line with the limited reciprocity of the EEC Prospectus Directive.[77] The letter further proposes to limit the application of any multinational offering regulation on "world class" issuers, at least in the initial stage.[78]

The ABA view reflects a deep mistrust of foreign disclosure principles by U.S. securities lawyers. The indispensable minimum supplemental information to be furnished according to the ABA is a description of the methodology of distribution in the particular foreign jurisdiction, a reconciliation of foreign accounting principles (like the one presently contained in Item 17 or 18 of Form 20-F), a "Management's Discussion and Analysis," and some open-ended additional information, including Regulation S-X, Item 18 segmented financials.[79]

The comment by Roberta S. Karmel, the former SEC Commissioner, seems similarly skeptical about abandoning segmented financials.[80] On

72. *Id.*
73. *See* Summary of Comments, *supra* note 21, at 23.
74. ABA-Letter, *supra* note 63.
75. *Id.* at 4.
76. *See* Summary of Comments, *supra* note 21, at 29.
77. ABA-Letter, *supra* note 63, at 5.
78. *Id.* at 7.
79. *Id.*
80. *See* Karmel, *supra* note 60, at 4, col. 4.

the other hand, any attempt to preserve U.S. GAAP as an indispensable disclosure item will severely hamper maximum reciprocity. Some European companies also expressed concern about segmented financials.[81] As will be seen, EEC law requires segmented reporting if the revenues are disproportionately distributed among different segments. The chance that any material information is withheld from the investors in the U.S. is minimal. What is more certain is that some supplemental information items are indispensable for the U.S. investor, notably information about currency exchange rates and exchange controls. Any such supplemental information required should, however, be absolutely indispensable in order to achieve maximum reciprocity.

The ABA additionally points out that other obstacles have to be overcome, like divergences in liability provisions, in the review procedure, and in periodic reporting.[82] The letter proposes a grace period for newcomers, having in mind that the most recent multinational offering, such as British Telecom and Reuter's, involved companies going public for the first time.[83] In addition the letter points out the divergences in the review proceedings that can involve delicate timing problems.[84] The letter also highlights problems of prefiling communications and the problems of arbitrage in the immediate aftermarket.[85]

Other comments seem to favor the reciprocity approach, but suggest a reconciliation of the financial statements with the accounting standards of the country where the security is offered.[86] Questions remain as to whether straight compliance with the present requirements of Item 18 should be required, or whether a financial statement according to the issuer's domicile plus a supplemental statement explaining the differences might be sufficient. The opinions expressed varied.[87] Some commentators apparently cautioned against proceeding too quickly and urged restraint in doing away with the present legal situation.[88]

Canadian securities regulators proposed a go-ahead of a U.S., Canadian solution with the chance of the U.K. joining later.[89] The inclusion of the U.K. in a multinational offering facilitation effort is, however, especially

81. *See* Summary of Comments, *supra* note 21, at 18, 37.
82. *See* ABA-Letter, *supra* note 63, at 10.
83. *Id.* at 12.
84. *Id.* at 12-13.
85. *Id.* at 14.
86. *See Multinational Securities Offerings Discussed at NASAA Annual Conference*, 17 Sec. Reg. & L. Rep. (BNA) 1752 (1985).
87. *See* Summary of Comments, *supra* note 21, at 33-34.
88. *See* ABA-Letter *supra* note 63, at 15.
89. *See* Summary of Comments, *supra* note 21, at 33-34.

desirable. The integration of the U.K. could prove to be an opener for a later version including the EEC as a whole.[90]

III. Initial Offerings in the U.K. before 1985

The U.K. can serve as an example of how an EEC directive is implemented into national law. In order to understand the effect of that implementation, and the present state of U.K. law, it may be helpful to look at the situation before 1985, the date on which the new U.K. listing regulations became effective. The difficulty is that the U.K. has three regulatory frameworks that overlap and intertwine.

A. The Companies Act of 1948

Under section 434 of the 1948 Companies Act, a company must register if there are more than twenty subscribers. Under sections 37 through 55, a prospectus has to be filed with the Registrar of Companies, and no security may be issued unless accompanied by a prospectus. The Stock Exchange, however, can under section 39 of the 1948 Companies Act, exempt a company from the statutory prospectus requirement. A company whose shares are traded on the Stock Exchange is subject to the Stock Exchange Regulations. In other words, the prospectus delivery requirement under the Stock Exchange Regulations will generally supersede the statutory obligation.[91] The Prospectus under the Stock Exchange Rules will fulfill the statutory requirements for disclosure under the Companies Act.[92]

B. The "Yellow Book"

The Stock Exchange Regulations are contained in a looseleaf binder with a yellow cover, hence, these regulations are usually referred to as the "Yellow Book."[93] The provisions are completely self-regulatory. The Stock Exchange is a private corporation and companies who want their shares to be traded must, by private agreement, comply with the Yellow Book. Before the transformation of EEC law in 1985, the Stock Exchange was completely free to grant exemptions from the provisions of the Yellow Book, as long as the statutory minimum disclosure standard was not

90. This position is also taken by Merloe, *supra* note 7, at 267.

91. *See* Morgan, *Admission of Securities to Listing*, 1985 J. Bus. L. 370, 371; J. Klages, Die Richtlinie der EG über den Börsenzulassungsprospekt 57 (1981).

92. *See* J. Klages, *supra* note 91, at 59.

93. *Id.*

undercut.[94] The Yellow Book disclosure standards are much stricter than the EEC standards. Nevertheless, since a waiver of disclosure requirements that go beyond the EEC standards is still possible,[95] the Yellow Book provisions do not pose a serious threat to harmonization efforts with regard to multinational offerings.

Distribution methods under the Stock Exchange Rules differ in part from U.S. underwriting methods. Four different methods exist for the distribution of securities; in all cases, however, a prospectus must be delivered.[96] A public issue can be offered without involvement of an underwriter. Called a "Public Issue by Prospectus," the issuer directly contacts the investing public. The investors subscribe directly with the issuer. This method works only for issuers already known to the public. Another offering method is the "Offer for Sale," where a so-called "Issuing House," i.e., an underwriter, assumes the task of distribution to the public. A third method is called a "Placing," where a broker buys the entire issue and then sells the stock subsequently to his clients. This method is permitted only upon special approval by the Stock Exchange, which is granted only if no public demand is expected. The last possible method of distribution is an "Introduction," a sale of a security that is already in the hands of the public.[97]

C. Antifraud Provisions

Under the Prevention of Fraud (Investments) Act 1958, a special prospectus liability is created, but securities listed on the Stock Exchange are exempt under section 14.[98] Another liability provision is, or rather was, contained in sections 38 and 43 of the Companies Act of 1948.[99] Section 38 covered the case of missing information, whereas section 43 covered false statements. Both provisions made liable the persons responsible for the prospectus, such as directors, promotors, and accountants. Reliance on expert opinion was a defense, as well as due diligence.[100] These provisions are still in existence in the new Companies Act of 1985, as sections 56, 66, and 67, but they do not apply to prospectuses for listed securities.[101]

94. *See* Morgan, *supra* note 91, at 371.
95. *Id.*
96. *See* J. Klages, *supra* note 91, at 59-60.
97. *Id.*
98. *See* Morgan, *supra* note 91, at 383.
99. *See* Welch, *Breach of Prospectus Requirements*, 6 Company Law. 247 (1985).
100. *Id.*
101. *Id.*

IV. The New U.K. Listing Regulations under EEC Law

A. The EEC Directives

The European Community makes fairly comprehensive efforts to harmonize company law in its member states.[102] Part of that effort is directed at the harmonization of the capital markets. The EEC has issued three directives that deal with capital market law: the Listing or Admissions directive promulgated March 5, 1979;[103] the aforementioned Prospectus Directive;[104] and the Interim Reports directive of February 15, 1982.[105] In addition there exists a draft directive on prospectuses for unlisted securities.[106]

1. *Nature and Effect of a Directive*

The EEC Treaty[107] establishes the goal of a Common Market, and one of the basic prerequisites for creating it is the harmonization of the law in the member states. Article 54(3)(g) of the EEC Treaty gives the council of ministers the power to coordinate the legal frameworks of the member states and to use directives to achieve that goal. The effect of a directive is laid down in article 189(3) of the EEC Treaty. According to this provision, a directive is binding on the state to which it is addressed, but the state has a discretion on how to implement it. An EEC directive is, therefore, supranational law. The order expressed by a harmonization directive is to enact legislation that gives effect to the substantive contents of the directive. As an example, article 3 of the Prospectus Directive states: "Member States shall ensure that the admission of securities to official listing on a stock exchange situated or operating within their territories is conditional upon the publication of an information sheet, hereinafter referred to as listing particulars."[108]

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102. *See generally* M. Lutter, Europäisches Gesellschaftsrecht 3-7 (2d ed. 1984); Merloe, *supra* note 7, at 256-60, 268-71.

103. *Council Directive of 15 March 1979 (EEC) No. 79/279*, 22 O. J. Eur. Comm. (No. L 66) 21 (1979) (coordinating the conditions for the admission of securities to official stock exchange listing).

104. *See supra* note 4.

105. *Council Directive of 15 February 1982 (EEC) No. 82/121*, 25 O.J. Eur. Comm. (No. L 48) 26 (1982) (information to be published on a regular basis by companies the shares of which have been admitted to official stock exchange listing).

106. *See supra* note 4 (disclosure requirements are almost identical to the ones contained in the *Prospectus Directive*).

107. Treaty Establishing the European Economic Community, March 25, 1957, 298 U.N.T.S. 11 (1958) [hereinafter EEC Treaty].

108. *Prospectus Directive, supra* note 4, at 2.

A directive is a unique creation of European law.[109] Whether directives that are not yet given legislative effect might have a "direct effect" is a matter of discussion.[110] The problem is that the deadlines given to the member states to implement the directives are almost never met. The deadline for the Prospectus Directive expired in 1982; the first country to give effect to the directive was the U.K. in 1985. In the case of harmonization directives that do not grant specific rights to the individual, it should, however, be fairly clear that the only addressees are the member states. Even though the directives can be fairly detailed, there is no obligation to copy them word for word; it is sufficient, if the substantive provisions are given effect.[111]

Under article 169 of the EEC Treaty the only way for the EEC Commission to enforce the directive is to initiate an enforcement action and, eventually, to sue the noncomplying country in the European Court of Justice.[112] According to article 171 of the Treaty, however, a judgment would be merely declaratory. The success of any harmonization effort is therefore entirely dependent on the good will of the member states.

2. *The Listing Directive*

The listing directive is basically intended to create uniform conditions for the admission of a security to the stock exchanges (article 4(1)). These conditions are only minimum conditions, and the member states are free to erect additional barriers for admission (article 5), subject, however, to the principle of equal treatment (article 7). The directive ensures that there is a competent authority to supervise compliance with the listing requirements (article 9) and that the public will have access to the information that is to be filed (article 17). These conditions are different for debt and equity and are contained in Schedules A and B, which define the minimum size of the company, the degree of distribution to the public, etc. If shares of a nonmember country are not traded at the stock exchange of the home country, admission is only possible if the securities are not barred from being traded there for the purpose of investor protection (Schedule A.II.B.).[113]

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109. M. LUTTER, *supra* note 102, at 5; *see also* Zuleeg, *Die Rechtswirkung Europäischer Richtlinien*, 1980 ZEITSCHRIFT FÜR UNTERNEHMENS- UND GESELLSCHAFTSRECHT 471.

110. *See generally* Easson, *The "Direct Effect" of EEC Directives*, 28 INT'L & COMP. L.Q. 319 (1979) (answer: it depends).

111. *See* Zuleeg, *supra* note 109, at 471-72.

112. For a more detailed exposition of the procedure, see Ebke, *Enforcement Techniques Within the European Communities: Flying Close to the Sun with Waxen Wings*, 50 J. AIR L. & COM. 685 (1985).

113. *See* Wooldridge, *Some Recent Community Legislation in the Field of Securities Law*, 10 EUR. L. REV. 3, 8 (1985).

Schedules B and C stipulate duties for the issuer to give the public at large access to financial information, usually by publication of the yearly balance sheet and a report on the present situation of the company, plus any material information likely to affect the market value of the securities (Schedules C.4. and C.5.). The information given to the public must be equal in all national markets where the security is traded (Schedule C.6.).

3. *The Prospectus Directive*

This directive requires the member states to make the publication of a "listing particular" a condition for listing at the stock exchange (article 3). Article 4 determines that the listing particulars must contain the information necessary to enable investors and their advisers to make an informed assessment of assets and liabilities, profits or losses, and prospects of the issuer. Article 4(2) also stipulates that the member states shall ensure that this obligation is "incumbent" on the persons responsible for the listing particular. Under articles 6 and 7 the competent authorities may grant an exemption from the disclosure requirements in specific cases. Article 6(e) mentions securities already traded on the stock exchange of a member state, but no exemption exists for which a U.S. issuer seeking access to a stock exchange in an EEC member country might qualify. Article 18 imposes a duty to appoint a competent authority to review the listing particulars before they are published, that is an agency very similar to the SEC.

If a listing particular is published or will be published, the issuer has to file all the other material published in connection with the offer, and the competent authority will decide whether these publications should be submitted to scrutiny before publication (article 22). The only substantive provision with respect to these prefiling communications is that they must state that a listing particular will be or is published and where it is available (article 22, second clause).

Under article 24(2) a listing particular requirement exemption can be granted under the condition that a previous offering in another member state occurred less than six months before and that a translation and supplemental information to comply with the requirements of the member state where admission is sought is furnished. This provision has to be read together with article 5, which sets forth that the disclosure requirements are mere minimum standards; the member states are free to require more, but not less, information. This approach is very similar to the ABA's proposed modified reciprocity approach. Schedules A (for stocks) and B (for bonds) set forth the substantive disclosure standards. Schedule A will be discussed below when it is compared to the U.S. disclosure standards. The provisions of Schedule B are almost identical.

4. *The Interim Reports Directive*

This directive imposes a duty on member states to ensure that issuers publish half yearly reports. The reports should at least contain tables on net returns and pre-tax and after-tax profits, and also appropriate comments (Article 5).

B. THE ACTUAL IMPLEMENTATION IN THE U.K.

Since the disclosure requirements in the Yellow Book are similar, but not identical, to those contained in the Prospectus Directive, it was not possible to implement the three directives by simply giving the Yellow Book statutory power.[114] The Yellow Book contains, for the most part, more stringent provisions.[115] Instead the U.K. chose to adopt the directive verbatim in the so-called Listing Regulations.[116] In turn, the Yellow Book was amended to include not only the Stock Exchange disclosure requirements, but also the legislative Listing Regulations, so that the Yellow Book is still a comprehensive enumeration of all applicable disclosure requirements.[117] Nevertheless, only the Listing Regulations have statutory power.[118] Since the admission to listing was self-regulatory before the Listing Regulations became effective, the issuer had to enter into a listing agreement. This requirement is now obsolete.[119]

The same applies to the prospectus requirement. Strangely enough, however, the new Companies Act of 1985, which consolidated the old 1948 Act, fails to refer to the new Listing Regulations, although it was enacted later.[120] Not yet clear (although likely) is whether the EEC prospectus will conform with the requirements of the Companies Act.[121] This matter is important when it comes to the question of what exhibits must be furnished and who has to sign the documents. Still an open question is whether compliance with the Listing Regulations will preempt application of the Companies Act.[122] The fact that the discretion of the Stock Exchange to grant waivers has been severely curtailed has been criticized.[123]

114. *Id.* at 7 n.19.
115. *Id.* at 7.
116. Morgan, *supra* note 91, at 371.
117. *Id.*
118. *See* Wooldridge, *supra* note 113, at 7.
119. *Id.* at 8.
120. *See* Morgan, *supra* note 91, at 378.
121. *Id.* at 380.
122. *See* Wooldridge, *supra* note 113, at 20 n.20.
123. *Id.* at 20.

An even more "ungodly jumble"[124] appears in the area of liability provisions. The U.K. apparently understood article 4(2) of the Prospectus Directive as imposition of a duty to implement a liability provision to ensure compliance with the disclosure requirements.[125] This idea is far-fetched, since article 4(2) merely states that the duty of compliance with the disclosure requirements has to be "incumbent" on the persons responsible for the prospectus. This wording does not indicate that a civil liability has to be created. A criminal liability or an administrative enforcement procedure would have done just as well. Be it as it may, section 5(2) of the Listing Regulations contains a civil liability provision, which, however, does not fit very well into the preexisting regulatory framework. The defense under section 5(2) is either lack of knowledge of the omitted facts, or an honest mistake of fact, or immateriality of the omission or falsity, as determined by the court.[126] The defenses under section 67 of the 1985 Companies Act are limited to due diligence.[127]

In addition, it is unclear who can sue under the new provisions of the Listing Regulations, and who can be sued as "responsible person." The issuer cannot be sued under either liability provision.[128] Under the Listing Regulations the liability is limited to the directors and presumably does not encompass accountants, lawyers, or others, since the directors are the only "responsible" persons under the Listing Regulations.[129] The question of who is liable is further complicated in the case of multinational offerings in several member countries. In other member states other categories of persons might be responsible. The question that arises is whether these persons will be liable in the U.K.[130]

The superimposition of the EEC directives onto the existing regulatory framework is consequently very problematic. While simple to do, it leaves to practice the task of working out the bugs. Probably for that reason, U.K. lawyers at present oppose the idea of a directive governing unlisted securities[131] in that it would probably destroy the remaining delicate balance in the U.K. system of securities laws.

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124. *See* Morgan, *supra* note 91, at 382.
125. *Id.; see also* Welch, *supra* note 99, at 248; Wooldridge, *supra* note 113, at 12.
126. *See* Welch, *supra* note 99, at 248.
127. *Id.*
128. *Id.* at 250.
129. *Id.* at 251.
130. *Id.* at 252.
131. *See* Sugarman, *Harmonization of Prospectuses: The Draft Directive on Unlisted Securities*, 3 COMP. LAW. 126, 127-28 (1982).

V. Tentative Synopsis of Disclosure under EEC and U.S. Law

In comparing the two disclosure systems under review, one has to keep in mind that the EEC directive does not directly address the problem of multinational offerings. Nor does it address offerings by foreign issuers. Since the disclosure requirements are mere minimum standards, they do not reflect the present disclosure requirements in the U.K. either. They do, however, reflect the minimum standards that cannot be undercut by waiver of the competent authorities. The requirements apply to foreign issuers as well as to domestic issuers. Compliance by issuers domiciled in other member states is easy, since the minimum disclosure is uniform. The member states are nevertheless free to add on additional requirements under article 5 of the Prospectus Directive, and the London Stock Exchange makes frequent use of that power.[132]

A. The Prospectus Format

Unlike the U.S. disclosure systems, the EEC Schedule A is not integrated with the continuous reporting provisions. The best way to compare both systems is to look at Form F-1 and Schedule A. Schedule A is divided into chapters with the headings: persons responsible for the listing particulars (Ch. 1), the admission to listing and the shares for which application for admission is made (Ch. 2), the general information about the issuer and its capital (Ch. 3), the activities of the issuer (Ch. 4), financial information (Ch. 5), administration, management, and supervision (Ch. 6), and recent developments and prospects (Ch. 7).

The information in Form F-1, in contrast, is divided into the following items: Forepart and Front Cover (Item 1), Inside Front and Back Cover Pages (Item 2), Summary Information, Risk Factors, and Ratio of Earnings (Item 3), Use of Proceeds (Item 4), Dilution (Item 6), Selling Security Holders (Item 7), Plan of Distribution (Item 8), Description of Securities to be Registered (Item 9), Interests of Named Experts and Counsel (Item 10), and Information about the Registrant (Item 11), which corresponds to Form 20-F under the 1934 Act.

Form 20-F is divided into the following parts: Business Description (Item 1), Description of Properties (Item 2), Legal Proceedings (Item 3), Control (Item 4), Trading Market (Item 5), Exchange Controls and Taxation (Items 6 and 7), Financial Data (Item 8), Management's Discussion and Analysis (Item 9), Directors and Officers (Item 10), Compensation (Item 11), Options (Item 12), Certain Transactions (Item 13), Description

132. *See* Wooldridge, *supra* note 113, at 7.

of the Securities to be Registered (Item 14), Defaults upon Senior Securities (Item 15), Recent Changes in Security (Item 16) and the Financial Statements (Items 17 and 18).

The integrated disclosure system makes the allocation of certain items more confusing than under the EEC prospectus format. Table 2 in the Appendix shows how the different items and chapters correspond to each other. The table shows readily that any reciprocity approach should either abandon disclosure based on a specific prospectus format, or should require a cross reference sheet. Such a cross reference sheet is obtained if Table 2 is reversed, as is shown on Table 3 in the Appendix.

B. SUBSTANTIVE DISCLOSURE

Achieving a complete match with respect to the information to be disclosed under the different systems is an illusory ideal. In some respects the U.S. requirements are more detailed, in other respects the EEC system seems more comprehensive. Table 2 shows that some items in Form F-1 have no correspondence in Schedule A. Dilution and Selling Shareholders (Items 6 and 7) are probably obsolete under the European system, since they apply only if a shareholder sells securities. The EEC regulation addresses only the issuer. Therefore a conflict between the two systems should not arise for U.K. issuers selling in the U.S. A U.S. issuer might not be able to coregister securities sold by shareholders.

Part 1 of Form F-1, the 500 series of Regulation S-K, is fairly identical to Chapters 2 and 3 of Schedule A. The only major difference is that the EEC provisions do not require a specific mention of risk factors. Certainly, the risk factors must be disclosed under EEC law, but they are not summarized at a specific place. The investor therefore has to make his or her own risk assessment based on the information scattered all over the listing particular, whereas Item 3 of Form F-1 requires the issuer to do this task. On the other hand, Schedule A.7.2. requires the issuer to discuss the prospects of the enterprise, whereas Rule 175[133] merely allows him to do so. Chapter 7.2. of Schedule A might also include an analysis of the risks of the particular investment. Both systems require disclosure of the capital of the issuer, the amount of underwriting commissions, the use of proceeds, and the plan of distribution.

More interesting are the divergences in the area of Form 20-F. In some respects, the dissimilarities are negligible, partly due to the fact that Form 20-F makes explicit reference to foreign disclosure requirements, such as in Items 11, 12, 13, and 17. Central to any disclosure is the description of the issuer and its activities. The European form is much more detailed

133. 17 C.F.R. § 230.175 (1986).

with respect to the participation of the issuer in "undertakings," that is, other enterprises and joint ventures. The financial situation of these undertakings has to be discussed extensively. Form 20-F merely requires a description of the issuer and its subsidiaries. Under EEC law, the undertakings have to be described in detail if they account for more than ten percent of the issuer's capital or profits (Schedule A.5.2.).

The U.S. disclosure requirements lay much more emphasis on the risk factors, as related to the particular enterprise or industry. The EEC directive never mentions the word "risk" in Schedule A. An example is Schedule A.4.2., where the issuer must disclose the dependency on patents, licenses, etc., "if such factors are of fundamental importance to the issuer's business or profitability."[134] The corresponding language in Item 1 of Form 20-F, states, inter alia, that the issuer must disclose "risk factors" such as "*expiration* of . . . patents, trademarks, licenses."[135]

Quite obviously, the leitmotiv of U.S. disclosure is the description of negative factors and a healthy skepticism about the mention of positive factors. In contrast, the European approach seems to be towards a more balanced and neutral disclosure with no specific emphasis on negative factors. In general, U.S. disclosure addresses more the lay investor and mandates the issuer to mark any risk factor as such. Under the European system, disclosure is aimed more towards the investor's adviser.[136] This targeting of the prospectus leaves it open to the reader to evaluate the risks involved in the investment and requires the investor to do his or her own risk analysis. The EEC approach seems more realistic. For the most part, the prospectus is read by professional investors or investment advisers. On the other hand, the risk factor analysis might be the only part of the prospectus that is actually read by the lay investor. The EEC approach has the disadvantage of lacking a specific section where all negative information is summarized and evaluated.

Under U.S. disclosure, the segmented reporting requirement that was originally relaxed in Item 1 of Form 20-F is reintroduced in Item 18. This segmented reporting is required in EEC law only if the operating results are atypically distributed among the different segments of the issuer's business.[137] The segmented reporting in the financial statements operates as a heavy burden on the foreign issuer. Besides this point of concern, the accounting principles in the U.S. and the EEC differ slightly, but have

134. *See Prospectus Directive, supra* note 4, at 22.

135. Form 20-F Item 1(b), 47 Fed. Reg. 54,781 (1982) (emphasis by the author).

136. *See Prospectus Directive, supra* note 4, art. 4(1) at 2.

137. *See Fourth Council Directive of 25 July 1978 (EEC) No. 78/660,* 21 O. J. EUR. COMM. (No. L 222) art. 43(1)(8) at 26 (1978) (contents of annual accounts and reports); *id.* § 3, at 13 (layout of the balance sheet).

the same overall intent of giving a fair view of the financial status of an enterprise.[138]

With the exception of some minor points of concern, the disclosures under both systems seem fairly similar with respect to management remuneration, the number of shares held by the management, and stock option plans. Both systems require disclosure merely of an aggregate amount. Form 20-F does lower the informational requirements with respect to the management's expertise, background, and outside activities.[139] The similarity in this area can be credited in full to the SEC's look to European securities law. With respect to disclosure of major shareholders, however, the provisions are still not in harmony even though Form 20-F relaxed the disclosure. Form 20-F still requires disclosure of any holder of more than ten percent of the issuer's stock, compared to five percent for domestic issuers. Schedule A sets the threshold at twenty percent, but in addition mandates the disclosure of any person exercising control over the issuer.[140]

VI. Conclusion: Feasibility of Transatlantic Multinational Offerings Facilitation

A. Divergence of Disclosure Standards

As shown above, the major philosophical difference between the EEC and U.S. disclosure is a stricter emphasis in the U.S. on negative risk factors. In contrast, the EEC provisions leave it to the investor to draw the appropriate conclusions. Nevertheless, the SEC's look to Europe has proven very helpful in achieving a limited harmony in disclosure standards. Some points, over which one may argue, make it more likely that supplemental information will be indispensable in order to protect the U.S. investor. As can be derived from the Summary of Comments,[141] a per se reciprocity without any supplemental disclosure is unrealistic. Even a modified reciprocity approach would be helpful, if it saves the expense of reformatting the information. To reorganize the prospectus format amounts to a complete redrafting, which is costly and time-consuming. Any approach under which the EEC prospectus can be furnished without redrafting, and supplemented by a "wrap around" prospectus, would already be a substantial facilitation.[142] Whether the ABA list of indis-

138. *See* Pierce, *supra* note 19, at 141.
139. Pierce, *supra* note 19, at 136.
140. *Compare* Form 20-F Item 4(b), 47 Fed. Reg. 54,771 (1982) *with* Schedule A.3.2.7., *Prospectus Directive, supra* note 4, at 11.
141. *See supra* note 21.
142. *See* Summary of Comments, *supra* note 21, at 29.

pensable information is an appropriate selection is, however, open to discussion.

As shown above, from the U.S. viewpoint, an explicit description of risk factors seems to be indispensable in order to bring an EEC prospectus in line with the U.S. philosophy of investor protection.[143] Yet, it seems that a Management's Discussion and Analysis is superfluous. This discussion is in most prospectuses a lengthy repetition of information contained elsewhere.[144] Whether a specific Methodology of Distribution should be discussed, is also debatable. This information should already be present in Schedule A.2.3.2., which provides that in multinational offerings, the reservation of a specific "tranche" to a particular country must be disclosed, as well as in other parts of Chapter 2.3.

The most important relaxation seems to be the abolition of the "increased financial disclosure" contained in Item 18. The ABA and others seem to cling to this information as indispensable.[145] The segmented financials are heartily disliked by foreign issuers.[146] Since the EEC accounting rules provide for disclosure in the case of atypical distribution of earnings among the different segments, the U.S. investor will still get the segmented information if it is important.

The essence of any reciprocity approach is to keep the amount of supplemental information as small as possible. Abolition of Item 18 seems to be one of the accommodations necessary to facilitate multinational offerings. It is hard to understand why Item 1 of Form 20-F substantially relaxes the requirement of segmented reporting, but fails to do the same thing with respect to the financial information in Item 18. Since Item 18-type financials are a prerequisite to taking advantage of the integrated disclosure system for most practical purposes, the relaxed segmented reporting is illusory at present.[147] As long as the financial information is reconciled with respect to the measurement principles, as presently provided in Item 17 of Form 20-F, a satisfactory investor protection is warranted.[148] Items of special interest for the U.S. investor are the exchange rate risk and the taxation risk. Therefore, Items 6 and 7 of Form 20-F should form part of the indispensable information.

As far as the reverse side of the coin is concerned—the accommodation of EEC disclosure to U.S. issuers—one has to keep in mind that Schedule A is not an administrative regulation that can be altered easily. Again, a

143. *Id.* at 39.

144. *But see id.* at 37-38.

145. *See* ABA-Letter, *supra* note 63, at 7; Karmel, *supra* note 60, at 4, col. 2.

146. *See* Summary of Comments, *supra* note 21, at 18 (*Royal Dutch and Shell*) 37 (*Unilever*).

147. *See supra* notes 57-62 and accompanying text.

148. *See* Summary of Comments, *supra* note 21, at 35-36 (the London Stock Exchange even expressed the view that any form of reconciliation of GAAP is unnecessary).

substantial accommodation may be achieved if the U.S. prospectus format could be used in a multinational offering in the U.K. securities market. With respect to the contents of the prospectus, only one supplemental information seems to be necessary to fulfill the disclosure requirements of the Prospectus Directive, namely a more thorough information with respect to the participation of the issuer in "undertakings" according to Schedule A.5.2.

Information about the future prospects of the issuer according to Schedule A.7.2. are part of the European disclosure philosophy, but this provision stipulates, too, that the competent authorities can grant a waiver from this requirement. For U.S. issuers, publication of forecasts is not part of their regular disclosure. Rule 175 is apparently not used very frequently. U.S. issuers apparently fear being held liable under section 11 of the 1933 Act if the forecasted results do not materialize. It would, therefore, be very helpful if the competent authorities generally exempted U.S. issuers from compliance with Chapter 7.2. of Schedule A.

As far as the format is concerned, it seems that the EEC directive does not really mandate compliance with the format of Schedule A.[149] Article 5(1) sets forth that member states shall ensure that "listing particulars contain, in as easily analyzable and comprehensible a form as possible at least the items of information provided for in Schedules A, B or C."[150] This wording is a clear indicator that the directive does not mandate a specific format. As a result, a U.S. prospectus, supplemented by information on undertakings, as suggested above, and a cross-reference sheet similar to Table 2 should be sufficient.

The question of to what extent the London Stock Exchange will accept such a prospectus and regard it as complying with the Yellow Book is beyond the scope of this article. However, the London Stock Exchange was one of the commentators that advocated a per se reciprocity approach.[151] The Exchange appears therefore, to accept U.S. disclosure as close enough to the requirements of the Yellow Book.

B. Other Areas of Necessary Harmonization

As the ABA-Letter and other comments indicate, the problem of multinational offerings does not hinge only on divergences in prospectus formats and contents. A successful solution should take into account the other stumbling blocks as well. In the area of disclosure requirements, harmonization seems easier to achieve, since at least in the U.S. a simple

149. *See* J. Klages, *supra* note 91, at 105.
150. *See Prospectus Directive*, *supra* note 4, at 3.
151. *See* Summmary of Comments, *supra* note 21, at 29.

modification of administrative regulations will be sufficient. This approach is for the most part not true with respect to liability provisions, problems of prefiling communications to the investors, and the problems of aftermarket regulation. This article discusses those issues briefly, although at least in some areas, a solution without congressional action seems unfeasible.

1. *Liabilities*

The liabilities provisions will always remain a major point of concern, and the SEC has declared any accommodation off-limits. Of course, any foreign issuer who offers securities in the U.S. will fear the harsh U.S. antifraud provisions regardless of whether the offering is multinational or not. Additional problems with respect to multinational offerings will, however, arise. Persons will become subject to liability who ordinarily are not involved in international securities offerings. The essence of a prospectus harmonization will be the use of opinions and exhibits prepared for the domestic market in a multinational offering. Experts, for instance, are not considered as "persons responsible" under the U.K. Listing Regulations. That does not mean that these persons are not liable under U.K. law; their liability is, however, dependent on negligence.[152] Under U.S. law, section 11(b)(3)(B) of the 1933 Act, the burden of proof would shift to the expert for due diligence. In addition, underwriters in the U.K. are only jointly, but not severally liable, which may also prove to be a deterrent for U.K. issues on the U.S. market.[153]

The multinational offerings arena will, however, in all likelihood, only be entered by sound companies where a liability case is highly unlikely to arise. If a multinational offering exemption is limited to "world class" issuers, the risks of a liability case are further eliminated. One commentator pointed out that the market forces would probably confine multinational offerings to "senior" or "world class" issuers.[154]

Liability, of course, depends to a large extent on the substantive disclosure requirements. In this respect the aforementioned slightly different emphasis on the disclosure of risk factors in the different systems might create a problem. A U.S. investor might sue on the ground that the U.K. prospectus did not specifically outline the risks of the investment, as required under U.S. law. On the other hand, a risk factor item should be part of the supplemental information package. In addition, an EEC prospectus must give an accurate picture of the issuer's situation. A case in

152. *See* the "classic" case of Hedley Byrne & Co. v. Heller & Partner Ltd., 1964 A.C. 465 (1963). For a discussion of the impact of *Hedley* see Welch, *supra* note 99, at 250.
153. *See* Summary of Comments, *supra* note 21, at 21.
154. *Id.* at 83.

which a prospectus might be deemed misleading under U.S. law, but not under EEC law is therefore unlikely. Hence, a multinational offerings facilitation will not be substantially impaired by existing liability provisions.

2. *The Underwriting and Filing Procedure*

The effect of pre-prospectus communications is a point of concern. Section 5(c) of the 1933 Act forbids these communications completely. The SEC cannot grant exemptions from the term "Offer for Sale" as defined in section 2(3). However, the SEC has rulemaking power under section 2(10) of the 1933 Act to exempt certain types of communications from the prospectus definition. Nevertheless the SEC has, in rule 135, defined the term "Offer for Sale" and has exempted "Tombstone Ads." The competent authorities in Europe have a similar discretionary power under article 22 of the Prospectus Directive. It seems feasible for the competent authorities to agree on an internationally acceptable form of prefiling communications in the case of intended multinational offerings.[155].

More difficult is the harmonization of the filing process as a whole in order to eliminate the intricate timing problems involved to achieve a simultaneous effective date.[156] Any delay in the review process might destroy the planned schedule of distribution. A close cooperation of all participating review authorities, as envisioned in article 24(1) of the Prospectus Directive is crucial, and an international multilateral agreement might be necessary to achieve that cooperation. One commentator showed that it is possible for a U.K. issuer to use the U.K. domestic subscription system in a multinational simultaneous offering in the U.S. if the sales are not made final before the "impact" day.[157] Another comment pointed out that the underwriting process in the U.K. is likely to become more similar to the U.S. type in the future.[158]

Another area of possible complications may arise from the different stabilizing possibilities in the separate capital markets. The immediate aftermarket might offer arbitraging opportunities.[159] A period of a couple of days, during which transborder transactions are prohibited, could prevent this problem. The difficulty is how such a prohibition might be created, and how it can be enforced. Self-regulatory measures of the national stock exchanges will probably be best.

155. *See also* ABA-Letter, *supra* note 63, at 15.

156. *See* ABA-Letter, *supra* note 63, at Appendix for a detailed description of the problems involved.

157. *See* Summary of Comments, *supra* note 21, at 89.

158. *Id.* at 88.

159. *See* ABA-Letter, *supra* note 63, at 15.

3. *Periodic Reporting*

A multinational offering facilitation is useless if the issuer is subsequently forced to comply with the 1934 Act reporting requirements; a filing of a Form 20-F at a later time would merely defer the moment at which the rewriting of disclosure information becomes necessary. If a foreign issuer will be subject to the 1934 Act filing procedure at some time, he might as well comply at the time of his first multinational offering. Any facilitation effort would lose its appeal without some sort of accommodation in the area of periodic reporting.

Commentators have expressed opposing views on the deterrent effect of the present periodic reporting requirements. At least two commentators have pointed out that a multinational offerings facilitation is ineffective without relaxations in the area of periodic reporting.[160] Since a European issuer (of world class, for example) has to file interim reports, information is available. Presumably, the larger the issuer is, the more information will be publicly available. It should suffice that an issuer files all these materials, as presently stipulated in Rule 12g3-2 for issuers of unlisted securities. A mere "grace period" as proposed in the ABA-Letter[161] will not suffice to render a multinational offering facilitation attractive. A "mirror image" modified reciprocity approach modeled after the multinational offerings facilitation in the periodic reporting area might, however, be a feasible way to enhance the attractiveness of a multinational offering facilitation.[162]

C. Outlook

A "modified" reciprocity approach appears to be the most feasible form of multinational offering facilitation; that is, a solution in which a domestic prospectus may be filed in conjunction with a supplemental "wrap around" prospectus containing the missing minimum disclosure.

With respect to the U.K., this minimum supplemental information should be limited to essential or indispensable items, such as: (1) a cross reference sheet similar to Table 3 in the Appendix; (2) a risk factors analysis; (3) a reconciliation of the financial statements with U.S. GAAP in a generic form, similar to the present Item 17 of Form 20-F; and (4) summary information about exchange controls and taxation. Information to be considered as dispensable includes (1) a Management's Analysis and Discussion and (2) segmented reporting, including segmented financials.

160. *See* Summary of Comments, *supra* note 21, at 74.
161. *Supra* note 63, at 11.
162. *See* Summary of Comments, *supra* note 21, at 74-75.

The deregulation of the London Stock Exchange ("Big Bang") has lured foreign securities firms to London, thereby increasing access for foreign investors to the U.K. securities market. While "Big Bang" affected secondary trading only, it remains to be seen whether increased foreign presence in the U.K. market will lead to an increase of international and multinational offerings. If this is the case, a multinational offerings facilitation will be helpful in fostering the ongoing internationalization of the world securities markets.

The SEC is apparently heading towards a relaxation for multinational offerings in the area of investment grade debt issued by world class issuers.[163] Such a precursor regulation should be broadened as soon as possible to encompass ordinary cash offerings of equity as well. A later inclusion of the EEC in general may be desirable and feasible.

163. *See* Address by SEC Chairman John Shad, at the National Press Club, Washington D.C. (Dec. 11, 1985) at 10 (copy on file with the author).

APPENDIX

Table 1
Appropriate Forms for Foreign Issuers under the 1933 Act

World Cl. Issuer:	Reporting Company for:	20-F filed:	Last 20-F included:	Type of Secs. offered:	Appropriate Form:
Yes	36 months	Yes	Item 18	Any Cash Offer	F-3
Yes	less than 36 months	One	Item 18	" " "	F-2
n/a	36 months	Yes	Item 17	Investment Grade nonconv. debt	F-3
n/a	less than 36 months	One	Item 18	Investment Grade nonconv. debt	F-2
No	36 months	Yes	Item 18	Any Cash Offer	F-2
Yes	36 months	Yes	Item 17	Rights Offering	F-3
Yes	less than 36 months	One	Item 17	" "	F-2
No	less than 36 months	One	Item 17	" "	F-2
n/a	not required	No	Item 18 (in F-1)	Exchange and residual cash off.	F-1
n/a	not required	No	Item 17 (in F-1)	Rights Offering	F-1

Table 2
Synopsis of U.S. and EEC Prospectus Formats*

EEC Prospectus Directive Schedule A	U.S. 1933 Act F-Series Form
Chapter 1	Form F-1 Signatures
Chapter 2	Form F-1 Items 4, 5, 8 and 9
	Form 20-F Items 5, 7 and 14
Chapter 3	Form F-1 Items 1 and 2
	Form 20-F Item 4
Chapters 4 and 5	Form 20-F Items 1 to 3, 8, 9, 17 (18)
Chapter 6	Form 20-F Items 10, 11, 12 and 13
Chapter 7 (part 1)	Form 20-F Item 9
Chapter 7 (part 2)	No Correspondence but see Rule 175
No Correspondence - F-1	F-1 Item 3 (Risk Factors)
	Item 6 (Dilution)
	Item 7 (Selling Shareholders)
	Item 10 (Interests of Named Experts)
No Correspondence - 20-F	Item 6 (Exchange Controls)
	Item 7 (Taxation)
	Item 15 (Senior Securities)
	Item 16 (Recent Changes in Security)

*For a more detailed synopsis on the basis of "old" Form 20-F see Pozen, *International Securities Markets*, 3 J. COMP. CORP. L. & SEC. REG. 199 (1981) (author: Douglas Hawes).

Table 3
Cross Reference Sheet

U.S. 1933 Act F-Series Forms	EEC Prospectus Directive Schedule A
Item 1	Chapter 3
Item 2	Chapter 3
Item 3	Chapter 5 (No Full Correspondence)
Items 4 and 5	Chapter 2
Item 6	No Correspondence
Item 7	No Correspondence
Item 8	Chapter 2
Item 9	Chapter 2
Item 10	No Correspondence
Item 11 (=Form 20-F)	*See* Below

U.S. 1934 Exchange Act Form 20-F	EEC Prospectus Directive Schedule A
Items 1 and 2	Chapters 4 and 5
Item 3	Chapter 4
Item 4	Chapter 3
Item 5	Chapter 2
Items 6 and 7	No Correspondence
Item 8	Chapter 5
Item 9	Chapters 5 and 7
Items 10 through 13	Chapter 6
Item 14	Chapter 2
Items 15 and 16	No Correspondence
Item 17 or 18	Chapter 5