

COMMITTEE ON CAPITAL MARKETS REGULATION COMPLETES SURVEY REGARDING THE USE BY FOREIGN ISSUERS OF THE PRIVATE RULE 144A EQUITY MARKET

NEW YORK, February 13, 2009 - The Committee on Capital Markets Regulation (“Committee”), an independent and nonpartisan research organization dedicated to improving the regulation of U.S. capital markets, has completed a survey regarding the explosive growth in the use by foreign issuers of the private Rule 144A equity market in the United States. This growth is especially striking compared to the shrinking use by foreign companies of the U.S. public equity market, as documented by the Committee’s quarterly updates of the competitiveness of the U.S. public equity market. Responses from counsel representing 17 of the 50 largest Rule 144A IPOs in 2007 identified five principal reasons for the growth in the private Rule 144A equity market: more developed home markets and increased liquidity outside the U.S.; the burdens imposed by the Sarbanes Oxley Act; the risk of securities class actions; compliance with U.S. GAAP; and increased liquidity in the Rule 144A market.

The Committee’s quarterly updates of the competitiveness of the U.S. public equity market (available at <http://www.capmksreg.org>) have shown an explosive growth in the use by foreign issuers of the private Rule 144A equity market, peaking in 2006 before the financial crisis. (Because the crisis has distorted equity and debt markets in 2008, we limit ourselves to data prior to 2008). Unlike public U.S. equity markets, the Rule 144A market is not subject to SEC regulation of public offering rules under the ’33 Act nor to ongoing regulation under the ’34 Act (including the Sarbanes-Oxley Act). Furthermore, the standard of liability for 144A offerings is lower than in the public market. Moreover, because access to this market is restricted to large institutions, the incidence of securities class actions is significantly lower.

Increased use by foreign issuers of the private Rule 144A equity market is evident in both the initial IPO decision and the overall amount of equity raised by foreign issuers in the Rule 144A market relative to U.S. public markets.

- Rule 144A IPOs by Foreign Companies
“Rule 144A IPOs”—IPOs by foreign companies listed outside their home country and privately offered in the U.S. pursuant to Rule 144A—account now for essentially all IPOs by foreign companies in the U.S. From 1996 to 2006, 64.1% of global IPOs by foreign companies (by value) in the U.S. were Rule 144A IPOs. By 2007, that figure had increased to 87.9%.
- Rule 144A Equity Privately Raised by Foreign Issuers in the U.S.
The value of Rule 144A equity privately raised in the U.S. by foreign issuers via American Depositary Receipts (“ADRs”) issued by the principal

depository bank—Bank of New York Mellon—has increased dramatically.¹ Averaging just \$0.9 billion in the period from 2000 to 2005, total Rule 144A equity ADR issuance by BONY reached \$9.9 billion in 2006 and was \$4.5 billion in 2007. These amounts, however, significantly understate total Rule 144A issuances because many foreign issuers now directly issue Rule 144A shares without using ADRs (consolidated data regarding these proceeds is not available).

- Relative Size of the Private Rule 144A and Public Equity Markets
In the period from 2000 to 2005, we estimate that foreign issuers raised on average 6.8% as much equity via Rule 144A ADRs as they raised in the U.S. public market. After spiking to 80.8% in 2006, the ratio declined to 24.0% in 2007. Again, because the Rule 144A ADR figures do not include Rule 144A equity directly issued by foreign issuers, these figures significantly understate total Rule 144A issuances by foreign companies.² Also, given the small amounts raised in either the public or 144A markets due to the credit crunch, current percentage shares probably are somewhat of anomaly.

While the data show an increased use by foreign issuers of the private U.S. Rule 144A market relative to the U.S. public markets leading up to 2006, the reasons for this dramatic switch in preference are not self-evident.

To better understand the increased preference of foreign issuers for the Rule 144A market, we interviewed counsel to those foreign companies who had elected in 2007 to make an initial equity offering in the U.S. privately pursuant to Rule 144A, rather than publicly on an exchange. We began by ranking the 50 top Rule 144A IPOs by foreign issuers in 2007 (by total offering value according to Dealogic). Of those, Dealogic identified the issuer attorney for 42 of the offerings. Of those 42 Rule 144A IPOs, we interviewed attorneys at 5 international law firms representing 17 of the largest Rule 144A IPOs.

We asked the attorneys the following questions:

- (1) Why did your client choose to raise equity outside of its home country?
- (2) Did your client consider an initial *public*—as opposed to a Rule 144A—offering in the U.S.?
- (3) What factors were important to your client in deciding to do a Rule 144A rather than a public equity offering in the U.S.?

¹ BONY's market share of newly created Rule 144A ADR programs has averaged approximately 60% in the period from 2000 to 2007.

² Another reason this ratio may be lower than the percentage of Rule 144A IPOs is because it reflects all—not just initial—capital raisings; it may be that IPOs are more likely to be Rule 144A eligible.

Respondents consistently identified five principal reasons for their use of the private Rule 144A market in the U.S.³:

- Developed home markets and increased liquidity outside the US: It is no longer necessary to tap the U.S. public equity market if one wants to make a public offering. Foreign issuers can get decent valuations at home, where local analyst cover is increasingly of high quality. Further, there is increased liquidity in foreign secondary markets. According to one respondent, “the US is no longer the only game in town.” It is much easier now to do a public offering at home or in another country and then to tack on a Rule 144A private offering in the U.S.
- Sarbanes Oxley Act: A listing on the the U.S. public market is now seen as creating too much regulatory risk, and regulatory requirements are perceived as excessively burdensome. According to one respondent: “A whole generation of dealmakers has grown up not having to deal with the SEC.” Although a U.S. listing used to be a “vanity listing,” reflecting the U.S. imprimatur, the Enron and Worldcom scandals changed that, and the U.S. “halo effect” has all but disappeared.
- Risk of securities class actions: The risk of securities class actions targeting public issuers was perceived as significant. This was particularly the case with respect to Chinese issuers following the experience of China Life, which was sued in a securities class action shortly after its initial listing in 2003. The litigation was traumatic for the Chinese government, and upper levels of government followed it closely, demanding detailed and up-to-date status reports. Subsequent to China Life, Chinese state owned enterprises were advised by the government to think very seriously before pursuing a New York listing and SOE listings in New York dried up.
- Compliance with US GAAP: Reconciling international financial reporting standards with US GAAP was seen as burdensome. This has now changed with SEC acceptance of IFRS without reconciliation, effective March 2008.
- Liquidity of Rule 144A market: Respondents pointed out that the market infrastructure for trading Rule 144A equity securities has dramatically improved, and has been particularly aided by the advent of new electronic trading platforms.

³ Country specific responses included differences in home country versus U.S. accounting treatment for proven natural resource reserves.