University of Miami Law School
Institutional Repository

University of Miami Law Review

11-1-1979

Transnational Offerings and the Problem of Integration

Seymour Arthur Casper

Follow this and additional works at: http://repository.law.miami.edu/umlr

Recommended Citation

Seymour Arthur Casper, *Transnational Offerings and the Problem of Integration*, 34 U. Miami L. Rev. 47 (1979)
Available at: http://repository.law.miami.edu/umlr/vol34/iss1/4

This Article is brought to you for free and open access by Institutional Repository. It has been accepted for inclusion in University of Miami Law Review by an authorized administrator of Institutional Repository. For more information, please contact library@law.miami.edu.

Transnational Offerings and the Problem of Integration

SEYMOUR ARTHUR CASPER

United States companies are offering their securities to foreign nationals in increasing numbers. Problems have arisen as to the applicability of various securities laws, especially the registration requirement, to such offerings. The author discusses the principal Securities and Exchange Commission releases and opinions which attempt to afford some relief but states that they only serve to confuse and obscure the problems.

A domestic corporation proposes to make a substantial dollar securities offering, part of which will be made to a select group of fifteen American investors and the balance to a large number of foreign purchasers. Will an issuer's claim for exemption, under section 4(2)[1] or rule 146,[2] from the registration provisions of the Securities Act of 1933[3] be adversely affected by the simultaneous sale to the foreign investors? Would it make any difference if the offers and sales to the American investors were not made concurrently with the foreign sales? If a domestic corporation makes a public offering of its securities partly to American investors and partly to foreign investors, will the issuer be required to register the entire offering under the Securities Act or just the portion being sold to the American group? Will the Securities and Exchange Commission (the "Commission") require a domestic issuer to register an offering made only to foreign investors, if they are all United States residents? Would it make any difference if such an offering were made entirely to nonresident foreign investors, or partly to nonresident foreign investors and partly to resident foreign investors? These questions assume added importance in view of the increased interest by foreign nationals in securities offerings by American companies both at home and abroad.

The relevant provisions of the Securities Act,[4] the rules[5] thereunder and the Commission's releases and letter rulings[6] as

1. 15 U.S.C. § 77d(2) (1976).
2. 17 C.F.R. § 230.146 (1978).
3. 15 U.S.C. § 77e (1976).
4. *Id.* §§ 77b(1), (3)-(4), (7)-(8), (10)-(11), 77e(a), (c), 77f-77g.
5. 17 C.F.R. §§ 230.146, .152 (1978).
6. Release No. 33-4708, 29 Fed. Reg. 9828 (July 9, 1964), Release No. 33-4552, 27 Fed. Reg. 11,316 (Nov. 6, 1962), Letter from SEC to Sulpetro Int'l, Ltd. (Aug. 25, 1977); Interpretative Letter to Salt Cay Beaches Ltd., [1974-75 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 79,985.

related to these questions, produce some strange results. The Securities Act provides that it is unlawful for a corporation to use the mails or instruments of interstate commerce to sell a security—unless a registration statement is in effect with respect to the securities,[7]—except when some exemption is available to the issuer. A violation of this provision could result in a civil suit by a purchaser of the unregistered securities,[8] an injunction action by the Commission,[9] or even a criminal prosecution.[10]

To determine whether an exemption from the registration provisions of the Securities Act is available, the issuer must consider, among other factors, whether the offering in question is in reality part of a larger offering. This brings into play the principle of integration espoused by the Commission.[11]

Take an extreme example of the problem—an offering by a domestic issuer to one sophisticated American investor and the simultaneous offering of the balance of the issuer's securities to some 300 foreign purchasers. In considering its sales to the one American investor, the issuer might expect to rely on the private placement exemption provided by section 4(2) of the Securities Act relating to "transactions by an issuer not involving any public offering."[12] The issuer must also, however, consider whether the concurrent offering to the foreign investors will be integrated by the Commission with the offer and sale to the one American investor so as to constitute a public offering which must be registered under the Securities Act.[13]

---

7. 15 U.S.C. § 77e (1976).

8. *Id.* § 77*l*. This section provides that any person who offers or sells a security in violation of § 5 is liable to the person purchasing the security, who may sue to recover the consideration paid for the security, or for damages if the purchaser no longer owns the securities.

9. *Id.* § 77t(b) (1976).

10. *Id.* § 77x.

11. *See* Release No. 33-4552, 27 Fed. Reg. 11,316 (Nov. 6, 1962).

12. 15 U.S.C. § 77(d)(2) (1976).

13. According to an eminent scholar in securities law, the private placement would be integrated with the foreign offering and the exemption claim under section 4(2) would be lost. Presumably, the issuer would be required to register the entire offering. H. SOWARDS, THE FEDERAL SECURITIES ACT (11 BUSINESS ORGANIZATIONS) 4-44.12(3) to .14 (1977). Professor Sowards states:

> [I]f the offering is made partly to persons in the United States and partly to persons in foreign countries, the *total* number of offerees must be considered in determining the availability of the exemption, whether the offering originates in this country or in the foreign country. For example, if *ABC*, Inc., a Delaware corporation, makes a one-million-dollar stock offering, part of which is purchased for investment by a selected group of 25 or less investment purchasers in this country and the remainder to 200 persons in Canada, *ABC*, Inc. has made a public offering.

Id. at 4-44.13 to .14.

Rule 152 under the Securities Act provides: "The phrase 'transactions by an issuer not involving any public offering' . . . shall be deemed to apply to transactions not involving any public offering at the time of said transactions although *subsequently thereto* the issuer decides to make a public offering and/or files a registration statement."[14] But to sustain such exemption, the subsequent offering must indeed be "separate and distinct" so as not to "constitute a single integrated raising of funds."[15] If the private placement were in reality a step preliminary to a public offering, the commission might integrate the two offerings and the exemption would be lost.[16] While the word "subsequently" in rule 152 has never been defined, many securities practitioners prefer waiting for a period of at least six months to one year after the private placement to avoid the possiblility of integration. Accordingly, rule 152 would seem to imply that if a public offering is made *simultaneously* with a private placement, integration would undoubtedly preclude any claim for the private placement exemption.

It appears, however, that a different conclusion is reached when offerings to foreign investors are involved. The Commission, in its release No. 33-4708, has stated, in effect, that it will not object to a domestic corporation publicly offering its securities abroad, solely to foreign investors, without registration under the Securities Act, provided the offering is designed to result in the securities' coming to rest abroad.[17] The Commission comes to this conclusion notwithstanding the definition of "interstate commerce" to include "trade or commerce in securities or any transportation or communication relating thereto . . . between any foreign country and any State, Territory, or the District of Columbia . . . ."[18] The Commission contends that because the Securities Act's principal purpose is the protection of American investors, it is not necessary to require registration in such a circumstance.[19]

14. 17 C.F.R. § 230.152 (1978) (emphasis added).

15. H. SOWARDS, *supra* note 13, at 4-44.13.

16. *Id.*

17. Release No. 33-4708, 29 Fed. Reg. 9828 (July 9, 1964).

18. 15 U.S.C. § 77b(7) (1976).

19. The exact language from the release is as follows:

However, the Commission has *traditionally* taken the position that the registration requirements of section 5 of the Act are *primarily* intended to protect American investors. Accordingly, the Commission has not taken any action for failure to register securities of United States corporations distributed abroad to foreign nationals, even though use of jurisdictional means may be involved in the offering. It is assumed in these situations that the distribution [of securities by a United States corporation] is to be effected in a manner which will result in the securities

If, however, such an offering allows for a high probability that the securities will be redistributed within the United States, registration may be required.[20] Thus, a foreign offering by a domestic issuer to Americans abroad would require registration.[21] Accordingly, if, in the course of an offering by a domestic issuer to foreign nationals, any securities fall into the hands of a single American investor, it would seem that the entire offering may become tainted and must be registered under the Securities Act. If this is the case, the Commission may need to be satisfied that all of the offerees or investors are indeed foreign nationals. A domestic issuer, then, should obtain from each foreign national an acknowledgment of such foreign status similar to the bona fide residency statement obtained from each offeree in an intrastate offering.[22]

Thus, because the Commission appears interested only in the protection of "American investors,"[23] would registration be waived for an offering by a domestic corporation to one hundred foreign investors, all of whom are resident aliens? Or, is a resident alien to be considered an American investor for this purpose? It is indeed difficult to conceive that the Commission would permit *any* offering of securities to be made within the United States or its territories, involving interstate commerce, without requiring registration under the Securities Act, regardless of the purchaser's nationality.[24]

Similar questions arise concerning an offering by a domestic issuer, part of which is to be made publicly to American investors and part of which is to be made to foreign nationals. Will the Commission require the issuer to register all the securities offered, or just those offered to American investors? Based on Release No. 33-

coming to rest abroad.

Release No. 33-4708, 29 Fed. Reg. 9828 (July 9, 1964) (emphasis added).

20. "On the other hand, a distribution of securities by a United States corporation, through the facilities of Canadian stock exchanges may be expected to flow into the hands of American investors and may therefore be subject to registration." *Id.*

21. *Id.*

22. *See* H. SOWARDS, *supra* note 13, at 3-43.

23. *Id.*

24. It is interesting to note, however, that the Commission's position as to foreign offerings by industrial companies is not carried over to foreign offerings by American mutual funds. The Commission has stated that a domestic mutual fund offering its shares in foreign countries must comply with all of the disclosure requirements of the Securities Act, including the furnishing of a prospectus. The Commission believes that since "[o]pen-end investment company shares, unlike for the most part other corporate securities, are vigorously merchandized abroad to large numbers of small investors from the public at large," such disclosure at the point of sale, as registration would require, helps protect the United States' securities market as a whole. This is accomplished by insuring that foreign investors will not seek redemptions because of later discovery that they had been inadequately informed about their investment. Release No. 33-5068, 35 Fed. Reg. 12,103 (June 23, 1970).

4708,[25] it would seem that only the securities offered and sold to American investors should be registered. But this writer is not aware of the Commission ever splitting an issue in this manner.[26]

The same release also appears to implement the suggestions of the Presidential task force concerning "simultaneous private placements in this country of a security being [publicly] offered abroad."[27] The task force recommended that when a domestic issuer makes a private placement in the United States simultaneously with a public offering abroad (presumably to foreign nationals), the Commission should consider granting the issuer's claim for exemption under section 4(2), with respect to the American offering.[28] This is conditional, of course, on the issuer's complying with section 4(2) or rule 146. In other words, the private placement within the United States would not be integrated with the public offering abroad, and the private placement exemption would not be lost, even though the two offerings are made concurrently.[29] Of course, this is contrary to

25. Release No. 33-4708, 29 Fed. Reg. 9828 (July 9, 1964).

26. By the same token, it would seem to follow that a foreign issuer making an offering, in part to American investors, and in part to investors in its own country, would be required to register only that part being offered to American investors. The Commission, however, has offered no definitive guidelines. It is also noteworthy that even though the foreign offering is not registered, a foreign purchaser may still be able to state a claim under the antifraud provisions of the federal securities law if misrepresentations were made in connection with the transaction. *See* Continental Grain (Austl.) Pty. Ltd. v. Pacific Oilseeds, Inc., [Current] FED. SEC. L. REP. (CCH) ¶ 96,767 (Feb. 6, 1979); Wandschneider v. Industrial Incomes, Inc., [1971-72 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 93,422 (Mar. 22, 1972).

27. Release No. 33-4708, 29 Fed. Reg. 9828 (July 9, 1964). The release states:

> As part of the program to reduce the United States balance of payments deficit and protect United States gold reserves, a Presidential Task Force on Promoting Increased Foreign Investment in the United States Corporate Securities and Increased Foreign Financing for United States Corporations Operating Abroad was appointed in October 1963. This Task Force was charged with developing programs for the increased foreign marketing of domestic securities, with particular emphasis on the securities of United States companies operating abroad, for a review of governmental and private activities adversely affecting such financing, and for an appraisal of the various barriers to such financing remaining in major foreign capital markets.

Id.

28. *Id.*

29. The relevant paragraph of the release states:

> The Task Force also suggests that the Commission's statement extend to simultaneous private placements in this country of a security being offered abroad. This specifically concerns the application of the exemption from registration provided by the second clause of section 4(1) of the Act for "transactions by an issuer not involving any public offering," the requirements for which were discussed in detail in Securities Act Release No. 4552 . . . . Generally, transactions otherwise meeting the requirements of this exemption *need not be integrated with simultaneous* offerings being made abroad and, therefore, are not subject to the registration requirements of the Act solely because a foreign offering

rule 152 and the Commission's view of integration previously discussed.[30]

Thus, Release No. 33-4708 represents an administrative modification of section 4(2) of the Securities Act. As illustrated by the Commission's reply to a letter of inquiry involving Salt Cay Beaches Limited,[31] this modification can produce an interesting result. The facts as related in the Salt Cay letter involved a foreign issuer, incorporated under the laws of the Turks and Caicos Islands, which proposed to offer 299 shares of its common stock ($1,000 par value) *"to various sophisticated investors throughout the world, including United States citizens and residents."*[32] Each investor was required to sign an investment letter prohibiting future resales until approval by issuer's counsel. A first right of refusal to purchase the issuer's securities was given to the issuer and then to its present shareholders. The issuer represented that its offering to the United States citizens and residents was intended to comply with rule 146 and that the total number of purchasers would not exceed thirty-five, as provided in paragraph (g)(1) of rule 146.[33] The issuer contended that for the purposes of rule 146, nonresident alien purchasers of the issuer's common stock should be excluded from the computation of the purchaser limitation of rule 146(g)(1). The issuer based its contentions primarily upon the Commission's alleged policy with respect to the applicability of the United States securities law to foreign purchasers of domestic securities as stated in Release No. 33-4708.[34] The Commission staff acknowledged its statements in Release No. 33-4708 and summarily agreed with the issuer's conclusions.[35]

Thus, the Commission staff's response to Salt Cay seems to permit a foreign or domestic issuer to find an exemption from the registration provisions of the Securities Act for a portion of an offering without fear of losing the exemption even if the balance of the offering is concurrently made to the public. This letter ruling, however, could be peculiar to the facts—a foreign public offering by a

---

is being made concurrently with the American private placement which otherwise meets the standards of the exemption.

Id. (emphasis added).

30. *See* text accompanying notes 14-16 *supra.*

31. Interpretive Letter to Salt Cay Beaches Ltd., *supra* note 6.

32. *Id.* at 84,531 (emphasis added).

33. Section (g)(1) of rule 146 provides: "There shall be no more than thirty-five purchasers of the securities of the issue from the issuer in any offering pursuant to the rule." 17 C.F.R. § 230.146(g)(1) (1978).

34. See notes 19-20 and accompanying text *supra.*

35. Interpretive Letter to Salt Cay Beaches Ltd., *supra* note 6, at 84,532.

foreign issuer and a simultaneous domestic private placement under rule 146. This ruling appears to be contrary to the Commission's position as expressed in Release No. 33-4552[36] relating to integration and rule 152.[37] This writer wonders if the Commission would respond similarly to a domestic issuer in the same circumstances.

In another no-action letter by the Commission staff dated August 25, 1977,[38] the staff also referred to Release No. 33-4708 in considering the following:

In 1975, Pellon Exploration, Ltd. ("PEL"), a Louisiana corporation and wholly-owned subsidiary of Pellon Corporation ("Pellon") of New York, acquired 50,000 shares of common stock of Sulpetro International, Ltd. ("SIL"), a Delaware corporation. These shares were acquired by PEL from shareholders who had acquired the same in a spin-off by SIL in 1973. An additional 375,000 shares were acquired by PEL in June 1976 through an offering by SIL pursuant to rule 146.

Pellon was wholly-owned by Freudenbog & Co., a West German limited partnership. The partnership had 150 members, 20 of whom were United States citizens or residents and 130 of whom were nonresident aliens. PEL proposed to sell all or substantially all of its SIL shares to certain nonresident alien partners of Freudenbog & Co. It also proposed to police the transfer of any such shares to assure that no resale would be made to any United States citizen or resident.

The Commission staff concurred with the issuer that the "proposed offering by PEL of the SIL shares would not affect the status of SIL's previous offering under Rule 146."[39] The Commission staff thus said it would not recommend any enforcement action if the proposed sale was made without compliance with the registration requirements.[40]

This letter ruling can be distingushed from the staff's ruling in regard to Salt Cay because the proposed offering by PEL (which is probably an affiliate of SIL by virtue of the amount of its stock ownership) of the SIL shares was not concurrent with the rule 146 private placement. In fact, PEL's proposed offering followed SIL's rule 146 private placement by a year or more. It would therefore appear that the problem of integration is not really an issue in this case.

36. Note 11 *supra*.
37. 17 C.F.R. § 230.152 (1978).
38. Letter to Sulpetro Int'l, Ltd., (Aug. 25, 1977).
39. *Id.*
40. *Id.*

Thus, an analysis of rule 152, Release Nos. 33-4708 and 33-4552, and the above letter rulings seems to indicate that the Commission has adopted two different positions: first, where there is an offering of securities by a domestic issuer, part of which is made pursuant to a private placement exemption from the registration provisions of the Securities Act and a simultaneous public offering abroad of the balance; secondly, where part of an offering is made pursuant to a private placement exemption by a domestic issuer and the balance is concurrently offered publicly, pursuant to a registration statement filed with the Commission. In the first situation, the exemption will not be lost through integration,[41] whereas in the second example, integration will probably be applied by the Commission to destroy any claimed exemption for an offering made concurrently with a public offering.[42]

The Commission, through its Chief of International Corporate Finance, recently confirmed its position by stating that, because Release No. 33-4708 has not been withdrawn or superseded, it "clearly indicates that no integration need be made in the circumstances outlined in the Release."[43] According to the Commission's letter, there will be no integration where a bona fide public offering outside the United States is made simultaneously with a bona fide private placement in the United States.[44] Although the phrase "bona fide" is not in Release No. 33-4708, it is assumed the Commission's reference to "a *bona fide* public offering outside the United States"[45] means an offering by a domestic issuer to foreign nationals *only* with all the necessary safeguards against any distribution or redistribution of the securities offered in the United States. The Commission's statement as such, not only does nothing to clear up the confusion and uncertainty surrounding the subject, but adds to it. The amount of time the issuer must police such an offering to retain its "bona fide" character is unclear. What will the Commission do if some securities (even small in amount) should be resold to American investors at home or abroad? Will the issuer's claim for exemption be retroactively lost? It would seem so.

Confusion also surrounds the extent of applicability of Release No. 33-4708. This writer assumes that "in the circumstances"[46] referred to in the Commission's letter is intended to confine applica-

41. *See* Release No. 33-4708, 29 Fed. Reg. 9828 (July 9, 1964).
42. *See* notes 14-15 and accompanying text *supra*.
43. Letter to Professor Hugh L. Sowards (on file *Unitersity of Miami Law Review).*
44. *Id.*
45. *Id.*
46. *Id.*

tion of the Release No. 33-4708 to a situation involving a claim for exemption under section 4(2) or rule 146 only and a concurrent foreign public offering. Why the task force and Commission should choose to limit this statutory modification in such manner is a puzzle to this writer. For example, would a claim for exemption under section 3(a)(11) or rule 147 while a simultaneous offering is made abroad or in the United States, be integrated? Would a regulation A filing be integrated with a concurrent foreign public offering? At present, The Commission's lack of guidance in this area seems to imply that in both instances, the entire offerings would have to be registered under the Securities Act. The current dilemma in this area raises many problems and leaves many more unsolved. All must await clarification by the Commission.