

# SEWARD & KISSEL LLP

July 15, 2021

## Testing the Waters: Tapping U.S. Capital Markets without SEC Registration by Cross-Trading on OTCQX International

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*The U.S. capital markets offer greater liquidity and deeper pool of sophisticated investors, skilled investment professionals and financial news and media outlets than any other market in the world. However, because of the fear of the registration with the U.S. Securities and Exchange Commission (the “SEC”), the cost of compliance with the U.S. federal securities laws, and the burden of meeting stock exchange cross-trading requirements, many international companies elect not to have their securities traded in the United States. OTCQX International provides a cost-effective way for smaller foreign private issuers<sup>1</sup> with securities cross-traded on a qualified foreign exchange to test the U.S. capital market waters and have their securities traded in the United States without SEC registration under the U.S. Securities and Exchange Act of 1934.*

### Exchange Act Registration

The U.S. Securities Exchange Act of 1934 mandates SEC registration by all companies, including foreign private issuers, that:

- have their securities cross-traded on a U.S. national securities exchange (NYSE and Nasdaq); or
- have assets in excess of \$10 million and securities held of record by either (i) 2,000 persons, or (ii) 500 persons who are not accredited investors<sup>2</sup>.

A company that has securities registered under the Exchange Act must make certain ongoing filings with the SEC under the Exchange Act and becomes subject to various other provisions of the U.S. federal securities laws. For example, a foreign private issuer must file with the SEC an annual report on Form 20-F, containing detailed financial and non-financial disclosure. Shareholders who acquire beneficial ownership of more than 5% of registered securities become subject to file with the SEC Schedule 13D or 13G reports, disclosing a variety of information. Under U.S. federal securities laws, a reporting foreign private issuer must: maintain books, records and accounts that “accurately and fairly reflect” its transactions and have in place a system of adequate internal

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<sup>1</sup> A foreign private issuer is an entity (other than a foreign government) incorporated or organized under the laws of a jurisdiction outside the United States unless: (i) more than 50% of its outstanding voting securities are directly or indirectly owned of record by U.S. residents; and (ii) any of the following applies: (1) the majority of its executive officers or directors are U.S. citizens or residents; (2) more than 50% of its assets are located in the United States; or (3) its business is administered principally in the United States.

<sup>2</sup> Accredited investors include: (i) certain US financial institutions such as banks, savings and loan associations, broker-dealers, and the like; (ii) corporations or partnership not formed for the specific purpose of acquiring the securities with assets over \$5 million; (iii) directors, executive officers, and persons holding similar positions with or in the issuer; (iv) natural persons with a net worth (alone or with that person’s spouse) exceeding \$1 million, excluding the value of the primary residence of the investor; (v) natural persons with individual income in excess of \$200,000 per year or, with that person’s spouse, in excess of \$300,000 per year; and (vi) any entity in which all the equity owners are themselves accredited investors.

accounting controls; not make corrupt payments to foreign officials; meet certain audit requirements; and comply with the Sarbanes-Oxley Act and its heightened compliance, disclosure and governance obligations.

Rule 12g3-2, however, provides two ways for foreign private issuers to be exempt from these requirements. First, Rule 12g3-2(a) provides that a foreign private issuer is exempt from Section 12(g) registration if its securities are held by fewer than 300 U.S. residents. Second, Rule 12g3-2(b) allows foreign private issuers of any size and with any number of shareholders to avail themselves of an automatic exemption so long as they satisfy certain conditions.

### **Rule 12g3-2(b) Exemption**

In order to take advantage of the Rule 12g3-2(b) exemption, the foreign private issuer must meet the following conditions:

- *No Existing SEC reporting.* The foreign private issuer has not publicly offered any of its securities in the United States or registered its securities under the Exchange Act;
- *Foreign cross-trading.* The foreign private issuer must maintain a cross-trading on one or more primary trading markets outside of the United States. Primary trading market means: (1) a foreign market that, either alone or together with another foreign market, accounted for at least 55% of the trading in the securities on a worldwide basis in the last fiscal year; and (2) if trading in two foreign markets is combined to meet the 55% threshold, the trading on at least one of them was greater than the trading in the United States;
- *Electronic publication of non-US disclosure documents.* The foreign private issuer must publish in English, either via its website or through an electronic information delivery system, information material to an investment decision that it has:
  - a. made public or been required to make public;
  - b. filed or been required to file with the stock exchange on which its securities are cross-traded and has been made public by the exchange; or
  - c. distributed or been required to distribute to its security holders.

Material information that should be disclosed includes: results of operations or financial condition; changes in business; acquisitions or dispositions of assets; the issuance, redemption or acquisition of securities; changes in management or control; the granting of options or payment of other remuneration to directors or officers; and transactions with directors, officers or principal security holders.

The Rule 12g3-2(b) exemption is a prerequisite for a foreign private issuer to have its securities quoted and traded in the over-the-counter markets, including OTCQX International, without SEC registration under the Exchange Act, ongoing reporting requirements and compliance various other provisions of the U.S. federal securities laws.

### **OTCQX International Quotation**

The OTCQX Best Market is the premium tier of the three stock markets operated by the OTC Markets Group Inc. in which over 11,000 U.S. and Global securities are traded. Through their wholly owned subsidiary OTC Link ATS, they connect a diverse network of broker-dealers that provide liquidity and execution services.

OTCQX International allows qualified foreign private issuers' to trade their securities through U.S. brokerage firms, the market makers. Similar to NYSE or Nasdaq listed securities, trades are settled in U.S. time zones using U.S. dollars. But unlike the NYSE or Nasdaq listed shares, quotation of securities on OTCQX International does not trigger the SEC registration requirement under the Exchange Act.

In order to qualify to have its securities quoted and traded on OTCQX International, without the Exchange Act SEC registration, a foreign private issuer exempt from registration under Rule 12g3-2(b) must meet the following additional eligibility standards:

- *Meet Initial Financial Standards.* To have securities quoted on OTCQX International, a foreign private issuer must one of the three tests: (1) at least \$2 million net tangible assets (or \$5 million if less than 3 years); (2) at least \$6 million average annual revenues; or (3) \$5 bid and one of (a) \$500,000 net income; (b) \$1 million net tangible assets; (c) \$2 million revenues; or (d) \$5 million total assets. Furthermore, the issuer must have a global market capitalization of at least \$10 million, a primary class of securities with a minimum bid price of \$0.25 per share and minimum of 50 beneficial shareholders, each owning at least 100 shares. For admission to a higher tier designated for larger companies, OTCQX International Premier, an issuer must have at least \$1 billion global market capitalization, average weekly trading volume of 200,000 shares or \$1 million over previous 6 months and 5 years of operating history.
- *Have Ongoing Operations.* A foreign private issuer applying for OTCQX International quotation must have ongoing operations and not to be a shell company or a blank-check company. It cannot be subject to any bankruptcy or reorganization proceedings.
- *Maintain a Cross-trading on a Qualified Foreign Stock Exchange.* A foreign private issuer must be cross-traded on a Qualified Foreign Stock Exchange for a minimum of 40 days. Over 70 markets have been designated by OTC Markets Group as Qualified Foreign Stock Exchanges (QFEs), including the following markets in the Nordic region: Nasdaq Copenhagen, Nasdaq Stockholm, Nasdaq Helsinki, Nasdaq First North, Nordic Growth Market, Spotlight Stock Market, Euronext Oslo Bors, Euronext Expand Oslo, and Euronext Growth Market Oslo. A complete list of QFEs may be found at <https://www.otcmarkets.com/corporate-services/qualified-foreign-exchange>
- *Make Rule 12g3-2(b) Information Publicly Available.* A foreign private issuer that relies on Rule 12g3-2(b) exemption must make publicly available by posting through the OTCIQ web portal/the OTC Disclosure & News Service last three annual reports and subsequent interim financial reports and other material disclosure subsequent to the most recent annual report required to be made publicly available by Rule 12g3-2(b).
- *Have Priced Quotes by a Market Maker on OTC Link.* A foreign private issuer needs to have proprietary priced quotations of its securities published by a U.S. market maker on OTC Link, an interdealer quotation and trade messaging system operated by OTC Markets Group.
- *Submit a Letter of Introduction from an OTCQX Sponsor.* A sponsor is an OTCQX qualified third-party service provider, an attorney, FINRA member or corporate broker. Keith Billotti of Seward & Kissel LLP has been designated as an OTCQX sponsor and can assist foreign issuers in determining OTCQX International eligibility, completing the application and compliance with OTCQX International rules.

In connection with the initial OTCQX International application, a foreign private issuer will need to submit an OTCQX International application, along with required supporting documentation, a company agreement and

pay a one-time application fee (currently set at \$5,000). To maintain the securities quotation and trading on OTCQX International, an issuer must pay an annual fee (currently set at \$23,000) and continue to maintain standards for continued qualification and satisfy ongoing disclosure obligations, including posting through the OTC Disclosure & News Service or an Integrated Newswire the information required to be made publicly available pursuant to Rule 12g3-2(b).

## **Testing the Waters and Tapping into U.S. Capital Markets**

OTCQX International provides an opportunity for foreign private issuers to test the waters and trade their outstanding securities in the U.S. capital markets without SEC registration under the Exchange Act, ongoing reporting requirements and compliance various other provisions of the U.S. federal securities laws. Quotation on OTCQX International allows foreign companies to grow and diversify their shareholder base and improve global liquidity<sup>3</sup> while raising their profiles among U.S. investors and investment professionals. Disseminating financial reports, material news and company research to a wider network of U.S. financial news and media outlets and U.S. broker screens may provide insight into the available liquidity and depth of market, including all broker-dealer bid and ask prices and sizes, and increase U.S. interest in a foreign issuer's securities. Consequently, foreign private issuers with securities quoted on OTCQX International may find it easier to tap into the U.S. capital markets and raise capital in the United States by issuing new securities either in a private transaction or a public offering.

Private transactions or offerings of securities to U.S. investors exempt from the U.S. Securities Act of 1933 registration requirements by a foreign private issuer typically would not affect such issuer's Rule 12g3-2(b) exemption or its OTCQX International status. However, any public offering of securities to U.S. investors would likely trigger the requirement to register the transaction with the SEC and the ongoing reporting requirements of the Exchange Act. Furthermore, any cross-trading of foreign private issuer's shares on the U.S. national securities exchange, NYSE or Nasdaq, would result in registration under the Exchange Act, ongoing reporting requirements and compliance various other provisions of the U.S. federal securities laws and the stock exchange cross-trading requirements. An OTCQX International company can withdraw its securities from OTCQX quotation at any time, upon 24-hours written notice to OTC Markets Group, and terminate it in connection with the cross-trading on the New York Stock Exchange or the Nasdaq Stock Market.

To learn more about cross-trading on the OTCQX Market, please contact Keith Billotti at [billotti@sewkis.com](mailto:billotti@sewkis.com) or your Seward & Kissel LLP relationship partner.

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## **About Seward & Kissel LLP Capital Markets and Corporate Securities Group**

Seward & Kissel is sought by issuers, investment banks and investors, including private equity sponsors, as a leading law firm in a broad range of capital markets transactions, including innovative and complex equity and debt instruments, offering structures, and public mergers and acquisitions. The Firm's Capital Markets and Corporate Securities Group has developed a reputation for its innovative and commercial approach to its client's capital needs. Seward & Kissel advises on nearly every type of capital markets offering. Issuers, investment banks and investors regularly rely on the Firm to help them raise capital through various securities products.

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<sup>3</sup> According to OTC Markets Group, a study conducted by Oxford Metrica that analyzed all international companies that joined OTCQX between 2007 and 2019 found that after joining OTCQX: (i) liquidity in the home market increased 26%; (ii) liquidity in the U.S. market increased 67%; (iii) 128 basis points of value was created for shareholders; and (iv) U.S. ownership more than doubled. Price and volume data were collected for each issuer one year prior to joining and up to three years after. In addition, US ownership data was collected one year prior and five years after.

## **About OTC Markets Group**

OTC Markets Group Inc. operates the OTCQX Best Market, the OTCQB Venture Market and the Pink Open Market for 11,000 U.S. and global securities. The OTC Link ATS and OTC Link ECN connect a diverse network of broker-dealers that provide liquidity and execution services, enabling investors to easily trade through the broker of their choice and empowering companies to improve the quality of information available for investors.

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