

New York Stock Exchange Major Global Regulatory Developments

Impact on Foreign Private Issuers in the U.S.

March 26, 2009

Executive Summary

Internal Control over Financial Reporting (ICFR)

- SEC has approved Interpretive Guidance for management regarding the design and evaluation of their ICFR, empowering management to take a top-down, risk-based, materiality approach.
- SEC and PCAOB have approved the elimination of the auditor's report on management's assessment of ICFR.
- PCAOB's audits are now conducted under Auditing Standard No. 5 (replaced Auditing Standard No. 2) - a new, streamlined auditing standard for auditor evaluations of ICFR, designed to eliminate unnecessary and duplicative work.
- SEC approved a one-year transition period for newly public companies, including Foreign Private Issuers (FPI) listing in the US for the first time: management and auditor ICFR reports will not be required until the second annual report filing with the SEC.
- Japan's Financial Services Authority (FSA) allows an SEC-registered Japanese company to use its ICFR report prepared in accordance with U.S. requirements for purposes of satisfying Japanese ICFR requirements.

Executive Summary (cont'd)

International Financial Reporting Standards (IFRS)

- As part of a cost-reducing regulatory trend toward Mutual Recognition, FPIs that prepare financial statements in accordance with IFRS as published by the International Accounting Standards Board (IASB), are no longer required to provide reconciliations to US GAAP, in their annual report (Form 20-F) as filed.
- SEC continues to research whether or not to allow US companies to file with IFRS-only financial statements and has published its much anticipated “Road Map” for domestic companies.

Executive Summary (cont'd)

Fast-Path Cross-Listing (Fast-Path)

- In a major step toward globalization of financial markets, European regulatory authorities will now allow use of existing SEC filed documentation for the purpose of constituting a European Prospectus compliant with the EU Prospectus Directive.
- Fast-Path enables NYSE-listed, non-EU issuers to cross-list on Euronext with or without capital raising, based primarily on existing documentation filed with the SEC.
- Fast-Path provides eligible companies with a convenient, cost-effective process to reach investors and gain strategic visibility in both the US and Europe, enabling the same security to be traded across continents, in multiple currencies, and in multiple time zones.

Internal Control over Financial Reporting (ICFR)

The Issues

- What were the major modifications to the auditing standards for ICFR and what guidance was issued for management?
- How have the changes affect listed companies and companies considering listing in the US?

SEC Guidance Approved (May 23, 2007)

- **Highlights**

- Interpretive Guidance for management regarding their ICFR evaluations – addressed many concerns:
 - excessive testing of controls; excessive documentation of processes, controls and testing; and ability to scale the evaluation depending on the company's size.

- **Based on two principles**

- **Efficiency:** Management should evaluate the design of controls that it has implemented to determine whether there is a reasonable (not absolute) possibility that a material misstatement in the financial statements would not be prevented or detected in a timely manner. Efficiency is promoted by allowing management to focus on material control items, including the role of entity-level and general information technology controls.
- **Alignment:** Management should gather and analyze evidence about the operation of controls being evaluated based on its assessment of risk associated with those controls and balance them with the greatest risks associated with financial reporting.

Highlights of SEC Approved Guidance

SEC Addressed Four Areas:

- Identification of risks to reliable financial reporting and the related controls that management has implemented to address those risks:
 - Requires more judgment on what is a material control and does not require that every control in a process be identified. Material misstatements due to fraud need to be considered as part of this risk based approach.
- Evaluation of the operating effectiveness of controls:
 - Provides for a risk based approach as management gathers and analyzes its evidence about the operating of its controls. Management can consider and utilize its daily interaction with its business, self-assessment and other ongoing monitoring activities to support its evaluation.
- Reporting the overall results of management's evaluation:
 - Management upon completion of its assessment needs to determine whether or not any of the identified internal control deficiencies are strong indicators of material weaknesses. Several examples of "strong indicators" are given in the guidance including: an ineffective control environment, restatements, identification by a new auditor of a material misstatement and for entities in a regulated industry, an ineffective regulatory compliance function.
- Documentation:
 - This relates to the nature and extent of evidential matter that management must maintain to support its assessment. This documentation can now take many forms and be presented in a number of ways and does not need to include all controls within a process that impacts financial reporting.

Highlights of SEC Approved Guidance (cont'd)

- **Comments on Impact of Interpretive Guidance**
 - Help make management's evaluation process more efficient and cost-effective.
 - In the absence of guidance, management had previously looked to PCAOB's auditing standard to conduct their evaluations, which was not the intended outcome. With this guidance, management could tailor and streamline their evaluation procedures to their company's unique circumstances.
 - SEC has not provided a checklist of steps to follow as the SEC is encouraging flexibility.
 - Rather the guidance describes a top-down, risk-based approach, allowing for the exercise of significant judgment so that management can design and conduct an evaluation that is tailored to its unique circumstances.
 - Management's subsequent efforts should be significantly less.
 - This is because subsequent evaluations should focus on changes in risks and controls rather than identification of all financial reporting risks and the related controls.
 - Further, in each subsequent year, the evidence necessary to reasonably support the assessment will only need to be updated from the prior years and not recreated anew.

Highlights of SEC Approved Guidance (cont'd)

- **Elimination of Auditor's Report on Management's Assessment:**
 - Requiring auditors to express a single opinion directly on the effectiveness of ICFR, rather than an opinion on the effectiveness and a separate opinion on management's assessment.
- **“Safe Harbor” for Issuers:**
 - Companies that conduct ICFR evaluations in accordance with new interpretative guidance can be assured that that is one way to satisfy their ICFR evaluation requirements. This new SEC guidance is not intended to disrupt current best practices, so companies can continue to follow their current procedures if they wish, provided they meet the requirements of this proposed standard.
- **Material weakness:**
 - Definition now codified: “A deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a ‘reasonable possibility’ that a material misstatement of the Company’s annual or interim financial statements will not be prevented or detected on a timely basis.”
- **Significant deficiency:**
 - Definition now codified to match PCAOB’s term.

PCAOB Approved AS5 (May 24, 2007)

Highlights

- **Replaced current PCAOB Auditing Standard No. 2 (Internal Controls) with new Auditing Standard No. 5 (Internal Controls).**
 - New standard is designed to focus the auditor on matters most important to internal control: eliminate unnecessary procedures; simplify and shorten the standard by reducing detail and specificity; and make the audit more scalable for smaller and less complex companies.
 - PCAOB has imbedded previous guidance into the rule language and has added descriptive notes as examples.
 - PCAOB also has added some additional rule making as it pertains to relying on the work of others and some administrative matters.

Highlights of PCAOB AS5

Much of PCAOB AS5 corresponds to NYSE Listed Company Working Group recommendations that were submitted to the PCAOB and SEC in June of 2006:

- **Remove the requirement to evaluate management's process:**
 - The extra audit opinion will no longer be necessary so this should assist in eliminating unnecessary and duplicative procedures.
- **Direct the auditor to the most important controls and stress the importance of risk assessment:**
 - A top down approach should focus on the financial statements and entity level controls with a focus on controls that can prevent and detect fraud. Allows auditors the ability to use more professional judgment in issuing key controls.

Highlights of PCAOB AS5 (cont'd)

- **Revise the definitions of "significant deficiency" and "material weakness", as well as the "strong indicators" of material weakness:**
 - Replaces several confusing and very broad terms such as "more than remote likelihood" and "more than inconsequential" with "reasonable possibility" and "significant" and allows for more auditor judgment in the evaluation of these areas.
- **Clarify the role of materiality:**
 - Should be applied at the financial statement level not the account level, although not formally defining what materiality is. However, it should be the same threshold for internal controls and the financial statement audit.

Highlights of PCAOB AS5 (cont'd)

- **Permit consideration of knowledge obtained from prior years' audits:**
 - Replaces the "every year must stand on its own" language and recognizes that there is significant value obtained from prior years' audits.
 - Direct the auditor to tailor procedures for smaller companies:
 - a more scalable approach and recognizes that the management of smaller businesses tend to be very involved in all day to day activities and allows the auditors to consider each company's unique facts and circumstances before applying the standard.
- **Refocus the multi-location testing requirements to focus on risk rather than "coverage":**
 - Testing should no longer focuses on the number of sites visited but rather allows the auditor to form a risk based strategy to focus on where the material activities of a business are conducted.
- **Allow the auditor to appropriately use the work of others:**
 - Eliminates the "principal evidence" provision and establishes a single framework based on the nature of the subject matter being tested and the competence and objectivity of the personnel performing the work, including at the control environment level.

One-Year Transition Period for Newly Public Companies

- **Newly public companies are not required to include either a report by management or an auditor's attestation report on ICFR in their first annual report filed with the SEC:**
 - SEC approved this transition period, which was proposed August 2006. Beneficiaries include foreign private issuers listing in the US for the first time. The management and auditor reports will be required in the second annual report filing with the SEC. The extra time will enable newly public companies to make implementation of ICFR reporting requirements more effective and efficient and will reduce the costs that a company faces in its first year as a public company.
- **Disclosure Required:**
 - Newly public companies relying on the transition rules must include statement in the first annual report that they file that the report does not include management's assessment report or the auditor's attestation report.

Subsequent Years Experience of US Companies

- US companies have completed four financial reporting cycles under the internal controls requirements of SOX.
- Surveys of US companies found that average costs drop in the second and third years of compliance.
- CRA International* found an average drop of 31% for small companies and 44% drop for larger companies (over \$700 million market cap). External ICFR auditing costs fell in the second year, but the two main drivers behind cost reductions were:
 - Efficiencies gained from the “learning curve” effect; and
 - First year documentation efforts didn’t need to be repeated in the second year.
- Financial Executives International found total compliance costs in the third year of compliance dropped about 35% versus year one, and largely attributed the drop to increased efficiencies after getting beyond the initial startup.

* The CRA International study was sponsored by the “Big Four” accounting firms.

International Accommodations for Cross-Border Listings

- **Japan:**
 - SEC-registered Japanese companies that obtain approval from the Financial Services Authority of Japan can prepare/file their ICFR report with the FSA in accordance with U.S. requirements generally without any reconciliations to Japanese ICFR requirements.
 - This development will potentially make it easier for Japanese companies to cross-list on NYSE and Tokyo Stock Exchange.

International Financial Reporting Standards (IFRS)

Background to SEC's Acceptance of IFRS

- NYSE has been an advocate of global accounting standards for many years.
- **Recent SEC progress on IFRS should be framed within the broader based trend toward Mutual Recognition:**
 - The concept of Mutual Recognition allows the SEC to recognize a non-US regulatory scheme as comparable to the US regulatory scheme. More than an exclusively “National Treatment” model, Mutual Recognition is better able to facilitate the ever-greater demand for global and cross-border investment opportunities.
- **The 2002 Norwalk Agreement reaffirmed in 2006 & 2008:**
 - The Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) agreed to make their existing financial reporting standards fully compatible “as soon as possible.”
- **IFRS for all European listed companies:**
 - That same year, the European Parliament and the Council of the EU determined to require all European listed companies to prepare their financial statements using IFRS in 2005.

Background to SEC's Acceptance of IFRS (cont'd)

- **Global Trend:**
 - Over 110 countries require or allow IFRS, and other countries are moving in that direction. However, there remain various national and regional interpretations regarding what IFRS is or should be.
- **Roadmap to IFRS in US for FPI's:**
 - In 2005, the SEC published its "Roadmap," committing the SEC to take steps to ultimately eliminate US GAAP reconciliations for FPI's reporting in IFRS.
- **SEC's proposal on IFRS for Foreign Private Issuers:**
 - In July 2007, the SEC proposed to accept financial statements from FPIs prepared using IFRS as published by International Accounting Standards Board (IASB), without reconciliation to US GAAP.
- **SEC approves acceptance of IASB-sponsored IFRS:**
 - FPIs that prepare financial statements in accordance with IFRS as published by the IASB, are no longer required to provide reconciliations to US GAAP, on their annual report on Form 20-F.
- **FPIs have a greater opportunity to reduce accounting costs:**
 - FPIs can now select one of three methods of preparing financial statements that are filed with the SEC: 1) US GAAP, 2) IFRS without reconciliation to US GAAP, or 3) another GAAP with reconciliation to US GAAP.

Highlights of SEC's Acceptance of IFRS (cont'd)

- **SEC has in the past considered use of IFRS by US issuers:**
 - In August 2007, the SEC issued a Concept Release on Allowing US Issuers to Prepare Financial Statements in Accordance with IFRS as published by IASB
 - In November 2008, the SEC published for comment its roadmap proposing the use of IFRS by U.S. issuers, with the aim of having most large U.S. companies making the transition by 2014.
- **SEC's decision to accept only IASB-sponsored IFRS for FPI's is very important:**
 - There remain various interpretations regarding what IFRS is or should be. Requiring a single version of IFRS is aimed at centralizing the accounting standard and standard setters in order to avoid the growth of various versions of IFRS.
- **SEC's action is a step towards a single set of globally accepted accounting standards:**
 - SEC believes that use of a common set of accounting standards will help investors understand investment opportunities more clearly and with greater comparability than if they had to gain familiarity with a multiplicity of national accounting standards, provided that the standards are of high quality, comprehensive and rigorously applied.

SEC Proposes Road Map for U.S. Issuers

- **August 2008 - issued with comment period, which was extended to April 2009.**
- **Key factors in determining success of global standards:**
 - Standards must be crafted in interest of investors
 - Standards setting process must be transparent
 - Standards setter must be independent
 - Standards setter must be accountable
 - International stakeholders must participate in standards setting process.
- **Possible early adoption for select companies based on specific criteria.**
- **Milestones to be evaluated by the SEC in 2011.**
 - Convergence efforts
 - IASB Foundation accountability and funding
 - IFRS data and tagging.
 - Accounting education and training.
 - Limited early use experience.
- **Phased-in approval by 2014 – 2016.**
- **New SEC Commissioner to review roadmap and deliverables.**

EU Accepts Third Country GAAPs

- **European Commission (EC) deemed certain GAAPs of non-EU countries as equivalent to IFRS as adopted by EU:**
 - The EC had been reviewing GAAPs of non-EU countries that had committed to converging with or adopting IFRS. The purpose of the review was to determine which of these GAAPs could be deemed equivalent to IFRS as adopted by EU.
 - On December 12, 2008, the EC determined to accept GAAPs of U.S. and Japan as equivalent to IFRS as adopted by the European Union (EU). The EC also determined to accept on a transitional basis GAAPs of Canada, China, India, and South Korea, and indicated it would review the situation of IFRS convergence in these countries by no later than 2011.
 - As a result, non-EU companies that prepare financial statements in accordance with GAAPs of U.S., Japanese, Canadian, Chinese, Indian or South Korea can list on a European regulated market such as Euronext without providing a reconciliation to IFRS as adopted by EU.

Fast Path Listing Procedure:

Cross-Listings in US
and in Europe

Fast-Path Cross-Listing in US and Europe

- **NYSE-listed global companies are cross-listed on Euronext**
 - There are 49 companies - including Royal Dutch Shell, Sanofi-Aventis, Companhia Vale do Rio Doce, IBM, and GE - with a combined market capitalization of approximately \$2.0 / €1.5 trillion (as of January 31, 2009).
 - Until 2008, NYSE listed companies seeking to cross-list on Euronext were required to prepare a European prospectus and comply with European post-listing disclosure requirements.
- **Converging disclosure and reporting obligations between US and EU has made cross-listing easier**
 - Cooperation between Euronext College of Regulators and US SEC has created a cost-effective procedure (“Fast-Path”) for SEC-registered companies, including non-EU foreign private issuers, to cross-list in both the US and Europe.
 - Fast-Path is possible because the EU Regulator will use SEC filed documentation – such as Form 20-F, Form F-1, and Form 6-K - for the purpose of constituting a European Prospectus compliant with the EU Prospectus Directive.
- **Fast-Path listing benefits for global issuers**
 - Enables issuers already listed on the NYSE or about to be listed, to conveniently and cost-effectively obtain a cross-market listing on NYSE Euronext in Europe. The procedure relies primarily on existing SEC filings.

Fast-Path Cross-Listing in US and Europe (cont'd)

- Enables NYSE-listed issuers to cross-list on Euronext with capital raising (an offering to qualified investors in Paris or a public offering in Amsterdam) or without capital raising.
- Enables shares or ADSs to be traded on one single cross-border trading platform with connectivity to Euronext's European stock exchanges of Amsterdam, Brussels, Lisbon, and Paris, in addition to trading on the NYSE in the US.
- Enables Issuers to strategically reach constituents across continents, and in multiple time zones and currencies (eg US Dollar, Euro, and others).



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Powering the exchanging world.™

Glenn Tyranski
Senior Vice President
NYSE Regulation
1-212-656-5142
gtyranski@nyx.com

Marc Iyeki
Managing Director
NYSE Euronext
1-212-656-5791
miyeki@nyx.com

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