Preparing Your 2013 Form 20-F

January 23, 2014

This memorandum highlights some considerations for the preparation of your 2013 annual report on Form 20-F. As in previous years, we discuss both disclosure developments as well as continued areas of focus for the U.S. Securities and Exchange Commission (**SEC**). In addition, we highlight certain U.S.-related regulatory actions and other developments of interest to foreign private issuers (**FPIs**).

Disclosure Developments for 2013 Form 20-F

While there has been no change in the actual Form 20-F requirements this year, below are selected disclosure developments worth highlighting for FPIs.

Conflict Minerals Rules

In our **Preparing Your 2012 Form 20-F** memorandum, we discussed SEC rules which implemented the Dodd-Frank Wall Street Reform and Consumer Protection Act (the **Dodd-Frank Act**) reporting requirements relating to "conflict minerals"—cassiterite, columbite-tantalite, gold, wolframite and other minerals determined by the U.S. government to be financing conflict in the Democratic Republic of the Congo or adjoining countries. Section 1502 of the Dodd-Frank Act and Rule 13p-1 under the Securities Exchange Act of 1934 (the **Exchange Act**) require all reporting companies, including FPIs, to make specialized disclosure and conduct-related due diligence about conflict minerals. No disclosure is required in the Form 20-F, but the conflict minerals disclosures are required to be contained in a new form, Form SD, to be filed by May 31 for the prior calendar year. The first required disclosure is due May 31, 2014 for calendar year 2013. These new rules are being challenged on several grounds, including under the First Amendment to the U.S. Constitution. On July 23, 2013, the U.S. District Court upheld the validity of the rules (see our client newsflash: **U.S. District Court Upholds Conflict Minerals Rules**), but on August 13, 2013, the plaintiffs appealed to the U.S. Court of Appeals. Oral arguments were heard on January 7, 2014. On January 10, 2014, the SEC posted the new **Form SD** on its website. Although the rules are being challenged, the rules have not been suspended pending outcome of the challenge, and the timing of a final decision is not known. As a result, companies, including FPIs, should consider what additional work may be needed to be in a position to comply by May 31, 2014.

Resource Extraction Rule

As discussed in our **Preparing Your 2012 Form 20-F** memorandum, the SEC also adopted a rule implementing the Dodd-Frank Act's reporting requirements relating to resource extraction issuers. For more information, see Davis Polk's client newsflash: **SEC Adopts Final Rules Implementing Dodd-Frank Disclosure Requirements for Resource Extraction Issuers**. Under the rule, an FPI that (1) files annual reports with the SEC and (2) engages in the commercial development of oil, natural gas or other minerals, is required to disclose the type and total amount of payments made by the company, its subsidiaries or entities under its control to a foreign government or the U.S. federal government for each "project" and each government in order to further the commercial development of oil, natural gas or minerals. Several groups filed a legal challenge which the U.S. District Court for the District of Columbia upheld. The court vacated the SEC's resource extraction rule and the SEC announced in September 2013 that it would not appeal the court decision, but will instead rewrite the rule through a new rulemaking process, taking into account the concerns expressed in the court's ruling. However, despite many anticipating a re-proposal of the rule, the SEC omitted the resource extraction rule from its 2014 **agenda**. It is unclear when new rules could be issued. As a result, there is no current obligation to provide such disclosure.

NYSE and Nasdaq Listing Standards for Compensation Committees

FPIs that follow their home country practice are exempt from various corporate governance requirements applicable to U.S. domestic issuers, including the compensation committee independence and compensation adviser requirements, provided that they disclose the significant ways in which their corporate governance practices differ from those followed by U.S. domestic companies. In our **Preparing Your 2012 Form 20-F** memorandum, we discussed the SEC's **final rules** relating to listing standards to implement the requirements regarding the independence of compensation committees and their advisers under the Dodd-Frank Act, which required each member of a listed issuer's compensation committee to be a member of the board of directors and to be "independent," as defined in the listing standards of the national securities exchanges. In December 2013, the SEC approved an amendment to Nasdaq's listing rules that govern the independence of compensation committee members. The rule change aligns Nasdaq's approach with that of the New York Stock Exchange (**NYSE**). Previously, the two exchanges diverged in how they treated directors who received any compensatory fees, including consulting and advisory fees. For Nasdaq-listed companies, a director who received such payments was prohibited from being considered independent for purposes of the compensation committee. The new rule replaces this strict prohibition with a requirement that the board of directors instead consider the receipt of such fees when determining eligibility for compensation committee membership, similar to the NYSE standard. For more information on the new Nasdaq requirements, see our client newsflash: **Nasdaq Proposes More Flexible Compensation Committee Independence Standards**.

SEC Disclosure Focus Areas

As in previous years, companies should keep the following SEC focus areas in mind when preparing their 2013 Form 20-F:

Financial Reporting and Audit Task Force; Internal Controls Over Financial Reporting

The SEC remains focused on issuers' internal controls over financial reporting. In July 2013, one of three new enforcement initiatives **announced** by the SEC was the creation of the Financial Reporting and Audit Task Force. The task force will concentrate on securities law violations relating to the preparation of financial statements, issuer reporting and disclosure and audit failures. In particular, in a December 2013 speech, the chief of the task force said that the task force is closely scrutinizing issuers' internal controls over financial reporting. In addition, on October 24, 2013, the Public Company Accounting Oversight Board (**PCAOB**) issued **Staff Audit Practice Alert No. 11** to address the significant number of audit deficiencies it has observed in the last three years relating to audits of internal control over financial reporting. The PCAOB suggests that audit committees: (i) discuss with their auditors any auditing deficiencies in these areas found through the auditors' own internal inspections or in PCAOB inspections; (ii) request information from their auditors about potential root causes in any areas of deficiency and (iii) ask how their auditors are addressing the matters discussed in the PCAOB Practice Alert and how involved senior members of the auditing firm are in those matters. The Deputy Chief Accountant at the Office of the Chief Accountant at the SEC also recently **questioned** whether all material weaknesses are being properly identified in companies' financial reporting. He suggested that this could be either because the deficiencies are not being identified in the first instance or otherwise because the severity of deficiencies is not being evaluated properly.

Management's Discussion & Analysis

As discussed in our **Preparing Your 2012 Form 20-F** memorandum, the SEC continues to focus on Management's Discussion and Analysis disclosure. FPIs should re-familiarize themselves with our previous advice as to key focus areas, including disclosure regarding liquidity and capital resources, material known trends and uncertainties and short-term borrowings.

Iran Threat Reduction and Syria Human Rights Act of 2012

In our **Preparing Your 2012 Form 20-F** memorandum, we discussed the new reporting obligations for companies under the Iran Threat Reduction and Syria Human Rights Act of 2012 (**TRA**). Public companies are required to include explanatory disclosure and make an IRANNOTICE filing on EDGAR if they or their affiliates knowingly engaged in certain Iran-related activities or transactions with persons designated for their support of terrorism or weapons of mass destruction proliferation during the period covered by the annual or quarterly report. For more information, see our client memoranda: **New Law Requires Issuers to Disclose Certain Iran-Related Transactions** and **SEC Issues Guidance on New Iran Disclosure Requirements**. The level of detail provided by issuers in their TRA disclosures has varied, but many have disclosed very minor activities. FPIs should have in place and document procedures for gathering the disclosable information. For example, we recommend that issuers send questionnaires to their affiliates and business units and include relevant questions in their D&O questionnaires.

More than 250 companies filed IRANNOTICES and related disclosures in 2013. The SEC has not issued any public guidance since the first round of disclosures pursuant to the TRA regarding trends it has observed or the quality of the disclosures it received in 2013. Further, despite the TRA's requirement that, with certain exceptions, the President investigate and determine whether to impose sanctions on an issuer or its affiliates for activities disclosed pursuant to the TRA, to date there has been no public statement indicating that the U.S. government has imposed sanctions on any company as a result of activities disclosed in SEC filings pursuant to the TRA.

In addition to the TRA disclosure obligations, the SEC has continued to focus on issuers' contacts with other countries besides Iran that have been identified as State Sponsors of Terrorism (*i.e.*, Cuba, Iran, Sudan and Syria). FPIs should consider relevant risk factor disclosure as well as other disclosure denoting the nature and materiality of contacts with sanctioned countries or those identified as State Sponsors of Terrorism.

Cybersecurity

In our **Preparing Your 2012 Form 20-F** memorandum, we discussed the SEC's 2011 **disclosure guidance** on cybersecurity risks and, in particular, on the need to provide more specific risk factor disclosure as to material cyber attacks that have occurred or specific threats to security in the future, without providing a roadmap on informational technology vulnerability. In April 2013, Senate Commerce Committee Chairman Rockefeller **asked** SEC Chairman Mary Jo White to elevate the Division of Corporation Finance's guidance to commission-level guidance. In her **response** on May 1, 2013, SEC Chairman White said SEC Staff have been reviewing whether companies have been disclosing enough information about their cybersecurity risks and protections. The SEC is using information gathered in that review to see if companies are complying with previously issued SEC guidance. Chairman White's letter indicates that the SEC is continuing to prioritize cybersecurity in its review of public company disclosures. More recently in October 2013, Chairman White **referred** to cybersecurity as a "hot topic from many perspectives." The SEC's continued focus on cybersecurity disclosures may signal that additional guidance is forthcoming or even suggest that more substantive regulations could be introduced in the future. Notwithstanding any further specific guidance from the SEC, and particularly for financial institution filers, we are expecting that there will at a minimum be enhanced risk factor disclosure relating to risks associated with cybersecurity attacks, risks associated with loss of data and reputational risks.

Accounting and Financial Reporting

Continued XBRL Relief for IFRS Filers

Consistent with prior years, until a taxonomy is specified by the SEC, FPIs that prepare financial statements in accordance with International Financial Reporting Standards (**IFRS**) as issued by the

International Accounting Standards Board (**IASB**) will not be required to provide financial information in an interactive data format using eXtensible Business Reporting Language (**XBRL**) as the SEC has not yet specified the XBRL taxonomy (see our client memorandum: **SEC Confirms IFRS Filers Will Not Be Required to Provide Interactive Data Until SEC Specifies Taxonomy**). This was **confirmed** by the SEC in September 2013, when it indicated that it is continuing to review taxonomies for use by FPIs. FPIs who are not providing XBRL information should not check the box on the cover page of Form 20-F relating to compliance with the interactive data file submission requirements.

The SEC has announced that an **Exposure Draft Interim Release Package on the IFRS Taxonomy 2013** was published by the IFRS Foundation and encouraged interested participants to participate in the review to assist the IFRS Foundation in continuing to develop the IFRS Taxonomy. The IFRS Taxonomy is a translation of IFRS into XBRL and interim releases contain additional taxonomy updates. The comment period for the draft closed on November 11, 2013. On January 15, 2014, the IFRS Foundation published for public comment **Interim Release Package 2**. The comment period closes on February 14, 2014.

Non-GAAP Financial Measures

In our **Preparing Your 2012 Form 20-F** memorandum, we discussed the SEC's continued focus on the use and disclosure of non-GAAP financial measures in SEC filings, company press releases and other public disclosures. Speaking at a December 2013 American Institute of Certified Public Accountants conference, the chief of the SEC's new Financial Reporting and Audit Task Force announced that the task force is now scrutinizing companies' use of measurements that do not comply with GAAP. Particularly, the task force is focused on examining companies' uses of non-GAAP indicators that conflate commonly used performance-indicating terms with "nonstandard measures" to enhance their standing and claim profits rather than losses in a way that could potentially mislead investors.

Other Matters That May Be Of Interest to FPIs

Foreign Corrupt Practices Act

In recent years, Foreign Corrupt Practices Act (**FCPA**) enforcement continues to be a high priority for the Department of Justice (**DOJ**) and the SEC. As discussed in our **Preparing Your 2012 Form 20-F** memorandum, the DOJ and the SEC issued **guidance** on the criminal and civil enforcement provisions of the FCPA. In a November 2013 **speech**, the Co-Director of the SEC's Enforcement Division noted that the SEC recovered over $240 million in disgorgement and penalties over the last twelve months and has filed over 40 FCPA enforcement actions over the past three fiscal years, and stated that the SEC will "remain the vigilant cop on the beat when it comes to the FCPA."

Social Media and Regulation FD

Regulation FD, applicable to U.S. domestic companies, prohibits "selective disclosure" by requiring public companies to disclose material information through broadly accessible channels, such as EDGAR filings, press releases and earnings calls. In July 2012, the CEO of Netflix, Inc., Reed Hastings, posted on his personal Facebook page congratulations on achieving a milestone: "monthly viewing exceeded 1 billion hours for the first time ever in June." Netflix subsequently announced in a Form 8-K that the company and its CEO each received a notice indicating that the SEC may bring action against them for an alleged Regulation FD violation. On April 2, 2013, the SEC issued as an Exchange Act release a **Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: Netflix, Inc., and Reed Hastings**. In the report, the SEC decided against pursuing an enforcement action against Netflix or its CEO. The SEC also affirmed that a company may use social media to communicate with investors without violating Regulation FD, so long as the company had adequately informed the market that material information would be disclosed in this manner. Although Regulation FD does not directly apply to FPIs, Section 202.05 of the NYSE Listed Companies Manual (the **Manual**) requires a listed company

to “release quickly to the public any news or information which might reasonably be expected to affect the market for its securities.” This was previously limited to press releases, but the NYSE rule now allows communication via any method that complies with Regulation FD, including social media. For more information, see our client memorandum: **SEC Explains How to Use Social Media for Regulation FD Compliance**.

SEC Issues Staff Report on Review of Regulation S-K

On December 20, 2013, the Staff of the SEC released its **report** regarding its review of the disclosure requirements in Regulation S-K, as required by Section 108 of the JOBS Act. Several senior SEC Staff, including SEC Chairman White and SEC Commissioner Daniel M. Gallagher, had previously referred to the report in their speeches criticizing the existing disclosure regime (see **SEC Chair White Addresses Possibility of Disclosure Reform** and **Commissioner Gallagher Promotes Changes to SEC Disclosure**). The chief accountant of the SEC’s Division of Corporation Finance also recently urged companies to scale back on unnecessary and duplicative disclosures and instead to focus on what is material to investors. According to the report, the overarching issues to be addressed include the possibility of principle-based disclosure rather than increasing static imperatives, scaling disclosure in accordance with different categories of issuers, a framework that distinguishes between “core” disclosure versus periodic disclosure and offering information, and improving readability while discouraging repetition. Potential reviews of the following were briefly addressed: (i) consolidating risk-based disclosure such as risk factors, legal proceedings and market risk disclosure; (ii) updating the relevancy of disclosures regarding businesses and properties; (iii) avoiding boilerplate for corporate governance requirements; (iv) addressing concerns that executive compensation disclosure is too long and technical and (v) making offering-related disclosure reflect the existing market. It is too early to assess the impact this report will have on how companies prepare disclosure documents going forward; however, if certain of these principles are adopted, it may also impact disclosures included in an FPI’s annual report on Form 20-F.

Committee of Sponsoring Organizations of the Treadway Commission

On May 14, 2013, the Committee of Sponsoring Organizations of the Treadway Commission (**COSO**) released its updated **Internal Control—Integrated Framework** (the **Framework**) and related illustrative documents. The Framework was first published in 1992 and is the leading guidance for designing, implementing and conducting internal control and assessing its effectiveness. The 2013 Framework is updated to account for the many changes in business and operating environments and clarify the requirements for determining what constitutes effective internal control. COSO suggests that users should transition to the updated 2013 Framework as soon as is feasible. However, COSO will continue to support the 1992 Framework until December 15, 2014. In addition, COSO suggests that issuers using the COSO Framework disclose for external reporting purposes whether they used the 1992 or 2013 Framework.

Nasdaq Modifies Listing Fees Payable by FPIs

On December 6, 2013, Nasdaq **modified** the listing of additional shares fee payable by non-U.S. companies. Under the previous rule, non-U.S. companies, including FPIs and non-FPIs, did not pay any fees for issuances of up to 49,999 shares per year and paid a flat fee of $5,000 for any amount of shares in excess of 49,999 shares issued during a year. Under the new rules, an FPI is now subject to increased listing fees of $7,500 per year for any amount of shares in excess of 49,999 shares issued during a year, effective January 1, 2014. Consistent with before, FPIs do not pay any fees for issuances of up to 49,999 shares per year. Non-U.S. companies that are not FPIs are now subject to the same fees as domestic companies, *i.e.*, an amount of $5,000 or $0.01 per share, whichever is higher, up to a maximum fee of $65,000 per year, for any amount of shares in excess of 49,999 shares issued during a quarter. There are no fees for issuances of up to 49,999 shares per quarter.

NYSE Affirmation

FPIs that are listed on the NYSE are reminded of the need to submit NYSE interim written affirmations promptly (within five business days) after the occurrence of a triggering event, which includes, among other events, the appointment and departure of directors and changes in the membership of board committees. In addition, FPIs are reminded that the NYSE annual written affirmation and chief executive certification is required within 30 days after the annual meeting.

Filing Fee Decreased

As of October 1, 2013, the filing fee to register securities with the SEC decreased to $128.80 per million dollars from $136.40 per million dollars. The SEC makes annual adjustments to the rates for fees and the annual rate changes take effect on the first day of each U.S. government fiscal year, *i.e.*, October 1.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

John Banes	**+44 20 7418 1317**	**john.banes@davispolk.com**
William F. Barron	**+852 2533 3303**	**william.barron@davispolk.com**
Maurice Blanco	**+55 11 4871 8402** **+1 212 450 4086**	**maurice.blanco@davispolk.com**
Julia K. Cowles	**+1 650 752 2007**	**julia.cowles@davispolk.com**
Michael Kaplan	**+1 212 450 4111**	**michael.kaplan@davispolk.com**
Nicholas A. Kronfeld	**+1 212 450 4950**	**nicholas.kronfeld@davispolk.com**
Jeffrey M. Oakes	**+44 20 7418 1386**	**jeffrey.oakes@davispolk.com**
Theodore A. Paradise	**+81 3 5574 2630**	**theodore.paradise@davispolk.com**
John J. Satory	**+44 20 7418 1027**	**john.satory@davispolk.com**
Michael J. Willisch	**+34 91 768 9610**	**michael.willisch@davispolk.com**

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