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LESS CAN BE MORE: RECENT EXAMPLES OF COOPERATION BETWEEN THE UNITED STATES AND EUROPEAN UNION ON SECURITIES REGULATION

I. INTRODUCTION

At least seventy percent of the global capital market lies on either side of the Atlantic.¹ Cooperative regulation of this transatlantic securities market thus has great potential to benefit businesses, investors, and—ultimately—consumers.² In addition to the sheer volume of transatlantic markets, their increasingly interconnected nature has of course also increased the need for cooperative securities regulation.³ Despite previous isolationist policies and unilateral strategies,⁴ officials from the United States and European Union have recognized this need and are fully aware that “[w]hat we need is a modern, open and reliable regulatory framework on both sides of the Atlantic.”⁵

1. Charlie McCreevy, European Comm’r for Internal Mkt. & Servs., *On the Road Towards Convergence and Equivalence—State of Play in International Accounting*, Speech Before the SEC Roundtable 4 (Mar. 6, 2007), *available at* <http://europa.eu/rapid/searchAction.do> (search complete database, reference “SPEECH/07/124”) [hereinafter McCreevy Speech, SEC Roundtable].

2. Charlie McCreevy, European Comm’r for Internal Mkt. & Servs., *Shifting up a Gear—Transatlantic Cooperation in Financial Services*, Speech Before U.S. Chamber of Commerce 2 (Mar. 6, 2007), *available at* <http://europa.eu/rapid/SearchAction.do> (search complete database, reference “SPEECH/07/125”) [hereinafter McCreevy Speech, U.S. Chamber].

3. As Ethiopis Tafara, Director of the U.S. Securities and Exchange Commission’s Office of International Affairs, explains, global securities markets have made international cooperation on securities regulation a true priority:

The ability to protect domestic securities markets turns on the ability to obtain and provide international cooperation. Capital markets today are increasingly global because: transactions transcend national boundaries with greater frequency and speed; public companies raise capital beyond their geographic boundaries; and investors trade outside their countries. Fraudsters are equally unconstrained by borders; they engage in illegal conduct in a multitude of jurisdictions, often simultaneously, and they transfer illegal proceeds to numerous jurisdictions in an effort to evade detection and prosecution. This globalization of fraud is a critical issue for every securities regulator, because illegal conduct which goes without detection or prosecution affects each and every one of our markets. It affects the confidence of our investors and their willingness to invest, and it affects capital formation. And, if aspects of the illegal activity can occur within any of our borders, without fear of detection, we can be assured that those who are inclined to engage in fraud will migrate to these vulnerable markets.

Ethiopis Tafara, Dir., Office of Int’l Affairs, Sec. & Exch. Comm’n Remarks Presented at the IMF Conference on Cross-border Cooperation and Information Exchange (July 7–8, 2004), *available at* <http://www.sec.gov/news/speech/spch070704et.htm> [hereinafter Tafara Speech].

4. *See infra* Part II A.

5. McCreevy Speech, U.S. Chamber, *supra* note 2.

The ubiquitous and grandiose rhetoric of globalization might suggest that cooperation should take on some unprecedentedly grand form or scope. But in reality this has not been the case. Globalization has proven not to be as monolithic as one might suppose, and recent examples of cooperation between the United States and EU on securities regulation have shown that there is no one-size-fits-all solution to the problems of fostering a transatlantic market. Specifically, changes in deregistration rules and accounting standards show that creating a workable transatlantic market does not require total uniformity in the administrative apparatus. Rather, in these situations the United States and EU have tailored their cooperative efforts—in terms of the intensity, level of commitment, kind of work, and stage in the regulation process when the activity takes place—to the particular issue at hand.

This Note examines the trend of collaboration in relation to two recent developments in securities regulation. The discussion begins with an explanation of the institutional and theoretical playing field, including a look at the actors involved in U.S.-EU securities regulation and some theoretical observations on transnational regulatory cooperation generally. The Note then analyzes two instances of cooperation between the United States and EU on securities regulation. First, with much input from the European Commission (“EC” or “Commission”), the Securities and Exchange Commission (“SEC”) recently loosened its rules on the deregistration of foreign issuers, a move resulting mainly from the passage of the Sarbanes-Oxley Act of 2002⁶ (“SOX”). Second, the SEC and European Commission are currently working toward mutual recognition of each other’s accounting standards. Finally, the note ends with a summary of the approaches taken and future prospects for cooperation between the United States and European Union on securities regulation.

II. THE INSTITUTIONAL AND THEORETICAL UNDERPINNINGS OF U.S.-EU COOPERATION ON SECURITIES REGULATION

A. *The Relevant Actors*

A discussion of cooperation on transatlantic securities regulation must, of course, begin by identifying the relevant actors on each side. Readers may be familiar with the SEC, which is responsible for enforcing

6. Sarbanes-Oxley Act of 2002, Pub. L. No. 107–204, 116 Stat. 745 (codified in scattered sections of 11, 15, 18, 28, 29 U.S.C.).

American securities laws.⁷ On the European side, the EC serves as the EU's "executive arm."⁸ It is divided into Directorates-General, each of which is responsible for a particular policy area. Thus, the Directorate-General for Internal Market and Services ("DG Markt") bears responsibility for securities regulation and generally "making the Single Market work."⁹

The EC, and specifically the DG Markt, is the SEC's most analogous counterpart. The Commission has broad executive powers,¹⁰ most notably the "right of initiative."¹¹ In exercising this right, it has the freedom to develop legislative proposals through a "relatively unstructured" process.¹² In fact, "[v]iewed from a U.S. perspective, the Commission and its Directorates-General appear to enjoy a high degree of autonomy in

7. The SEC has authority to enforce securities statutes, including the Securities Exchange Act of 1933, the Securities Exchange Act of 1934, and the Sarbanes-Oxley Act of 2002. U.S. Sec. & Exch. Comm'n, *The Investor's Advocate: How the SEC Protects Investors, Maintains Market Integrity, and Facilitates Capital Formation*, <http://www.sec.gov/about/whatwedo.shtml> (last visited Jan. 13, 2008). This Note assumes readers have basic familiarity with the SEC's rulemaking and enforcement authority.

8. European Union Institutions and Other Bodies: The European Commission, http://europa.eu/institutions/inst/comm/index_en.htm (last visited Jan. 5, 2008) [hereinafter *The European Commission*].

9. European Union, Directorate-Gen. Internal Mkt. & Servs., *Our Mission*, http://ec.europa.eu/dgs/internal_market/mission_en.htm (last visited Jan. 13, 2008). The mission of this Directorate-General states:

[T]he Internal Market and Services Directorate-general [sic] is directly responsible for proposing and—once laws are adopted by the European Parliament and Council—controlling the implementing of a European legal framework in the following specific areas: regulated professions, services, company law and corporate governance, public procurement, intellectual and industrial property and postal services. In the area of financial services, it aims at establishing the legal framework for the integration of the Union's capital markets and the creation of a single market for financial services.

Id. For ease of reading, this Note often refers to the DG Markt as the EC or Commission generally.

10. The Commission is "responsible for implementing the decisions of [the European] Parliament and the [European] Council." *The European Commission*, *supra* note 8. As a result, the Commission plays the kind of integral role in running the EU that agencies play in America—it is responsible for "managing the day-to-day business of the European Union: implementing its policies, running its programmes and spending its funds." *Id.* The Commission has four major roles: proposing legislation to the European Parliament and Council, managing and implementing EU policies and budgets, enforcing EU law, and representing the EU on the international stage so it can speak with "one voice" in international forums. In fulfilling these functions, the Commission answers to the European Parliament and President. *Id.*

11. Though the Commission functions similarly to American agencies in many respects, the right of initiative is a major exception. According to this principle, the Commission is the only body that can propose new legislation to the European Parliament and Council, so in addition to its typically executive powers, the Commission has some powers which an American might consider "legislative." *Id.*

12. George A. Bermann, *Regulatory Cooperation Between the European Commission and U.S. Administrative Agencies*, 9 ADMIN. L.J. AM. U. 933, 944–45 (1996).

determining how to formulate a draft regulation or directive.”¹³ Thus, although the Commission’s power differs in some aspects from that of U.S. agencies, it has at least as much authority as its American counterparts and enough autonomy to be able to negotiate on behalf of the EU.

The SEC and EC are institutionally well situated for cooperation. Each has a sub-unit dedicated to transatlantic or international relations. The SEC has formed an Office of International Affairs, and the EC has both a Commissioner dedicated to external relations and a delegation in Washington, D.C., to represent it in its business with the U.S. government.¹⁴

The two bodies have often reiterated their desire to cooperate. This rhetoric dates back to 1990, when the United States and then-European Community signed the Transatlantic Declaration on U.S.-EC Relations, which gave formal authority for a U.S.-EC partnership.¹⁵ In order to achieve their common goals, the parties pledged to “inform and consult each other on important matters of common interest, both political and economic, with a view to bringing their positions as close as possible, without prejudice to their respective independence.”¹⁶ The Declaration is full of globalization-era buzzwords and phrases, invoking no less than the “well-being of all mankind” and the “preservation of peace and freedom” at the end of the Cold War.¹⁷ But following such strong words, the Declaration lays out a “framework for consultation” without any specific goals for action on the agency level.¹⁸

13. *Id.*

14. European Comm’n, The EU’s Relations with the United States of America: Overview, http://ec.europa.eu/external_relations/us/intro/index.htm (last visited Jan. 13, 2008). The Commission has also sent a delegation to New York City, to serve as its observer at the United Nations.

15. Transatlantic Declaration of 1990, U.S.-E.C., Dec. 1990, *available at* http://useu.usmission.gov/Dossier/TransAtlantic/Dec1990_Transatlantic_Declaration.asp [hereinafter Transatlantic Declaration].

16. *Id.*

17. *Id.* The preamble to the Transatlantic Declaration notes that the parties recognize: “that the transatlantic solidarity has been essential for the preservation of peace and freedom and for the development of free and prosperous economies as well as for the recent developments which have restored unity in Europe” and are aware “of their shared responsibility, not only to further common interests but also to face transnational challenges affecting the well-being of all mankind . . .” *Id.*

18. *Id.* The Transatlantic Declaration provides a brief “Institutional Framework for Consultation,” which focuses on cooperation at the highest levels of government—the President and Cabinet on the U.S. side, and the President of the European Council, the President of the European Commission and the European Community Foreign Ministers on the European side. This focus misses the fact that issues like securities regulation are perhaps most easily and effectively resolved through negotiations between the individual agencies responsible for the specifics of an oversight regime. Thus, apart from creating a positive environment for cooperation, the Transatlantic Declaration does not play a large role in day-to-day cooperation on securities regulation.

This official policy of cooperation is further complicated by the SEC's history of isolationist and unilateral policies.¹⁹ Originally, the SEC acted on the assumption that "if a foreign issuer was going to tap the U.S. capital markets, it should play by the SEC's rules."²⁰ At that time, "the [SEC] did not give too much consideration as to how [its] expansive extraterritorial application of the securities laws would play out in foreign countries, or how legitimate foreign issuers would interpret the application."²¹

By the late 1970s and early 1980s, the SEC recognized that circumstances had made a cooperative approach more appropriate.²² Since then, the SEC has taken a more internationalist approach, focusing on comity with other states' regulations and accommodating the needs of foreign issuers. Yet this internationalist approach did not carry over to the SEC's requirement that foreign issuers comply with the provisions of SOX and make financial reports using the U.S. Generally Accepted Accounting Practices ("U.S. GAAP"), a U.S.-specific financial reporting standard.²³ Indeed, one former SEC Commissioner has accused the SEC of "frequently presum[ing] that U.S. standards are superior to standards abroad—an attitude that is greatly resented overseas."²⁴

In general, then, the SEC and EC seem to want an institutional policy centered around cooperation, but they have had difficulties realizing this policy in specific terms.

B. How International Regulatory Cooperation Works

International regulatory cooperation is not a one-size-fits-all solution. The result of effective regulatory cooperation is not necessarily (nor should it necessarily be) a single, international regulation and enforcement process.²⁵ In fact, as this Note will show, even within the limits of

19. For a brief history of the SEC's policies toward foreign issuers, see Roberta S. Karmel, *The Securities and Exchange Commission Goes Abroad to Regulate Corporate Governance*, 33 STETSON L. REV. 849, 852–57 (2004).

20. *Id.* at 853.

21. *Id.* at 854.

22. *Id.* at 855. These circumstances included the development of the European securities market and the desire to keep markets in London from competing with U.S. capital markets, the SEC's ability to be flexible in processing foreign-issuer disclosure documents for formerly state-owned enterprises in the U.K., the emergence of an international regulatory body, better securities disclosure and regulatory systems in foreign countries, and increased cooperation between the SEC and its foreign counterparts. *Id.*

23. *Id.* at 855–56.

24. *Id.* at 886.

25. Of course, it is sometimes preferable for states to cede their authority over a policy area to a supranational body or to adopt uniform regulations and enforcement policies. This Note argues,

securities regulation, the type and stage of cooperation depends greatly on the result sought.

Anyone seeking to criticize the efforts of the SEC and EC could easily point to documentation of the low intensity and commitment in their cooperation. For example, George Bermann has described methods for determining states' actual commitment to cooperation.²⁶ He asserts that, at least as of his writing in the mid-nineties, "[t]hose Commission services that have chosen to engage in programmatic cooperation with counterpart U.S. authorities have mostly steered away from high-intensity, high-commitment forms of programmatic cooperation."²⁷

however, that in many—perhaps even most—situations, lock-step similarity throughout the entire regulatory process is unnecessary. In fact, the policy goals which led states to regulatory cooperation in the first place may be served just as well by equivalent yet differing standards, or by cooperation in only one aspect of the regulatory process.

26. Bermann, *supra* note 12, at 961–62. Bermann lists several factors for determining parties' commitments to cooperation:

- (a) whether participants commit to collaborating,
- (b) whether they meet at regular intervals, with agendas,
- (c) whether the collaboration entails the occasional sharing of information and exchange of views, on the one hand, or a determined effort to reach common positions on the other,
- (d) whether the determined effort entails a further commitment to implement what is agreed upon,
- (e) whether deliberations are preceded by joint research and study,
- (f) whether what is contemplated are minimum standards or maximum standards or both,
- (g) whether and to what extent formal interventions in each other's domestic rulemaking processes are envisaged, and
- (h) whether participants engage in systematic follow-up on questions of implementation.

Id.

27. *Id.* at 962. Note that Bermann himself focuses more on describing efforts at cooperation than on critiquing them. The kind of "high-intensity" means of cooperation that Commission and U.S. officials usually rule out include "(a) the creation of full joint study teams, (b) parallel initiation of identical regulatory proposals, [and] (c) a program of formal written intervention in the other's regulatory processes." *Id.* Moreover, cooperation is more likely to succeed when it begins at an early stage in the regulatory process. Coordination from an early stage lessens the chance that regulatory disagreements will occur in the first place. This is because the parties involved are less likely to have committed themselves to a regulatory position at that point. Also, "[s]harp differences in rates of progress toward a common goal can in fact be a cause of friction in international regulatory cooperation efforts," and it is less likely at the beginning of the process for one party to have progressed significantly further than the other. *Id.* Note that cooperation need not start with the first phase (policy development); it is merely more likely to succeed when the parties enter a particular phase in the regulatory process at the same time. So, for example, regardless of how long ago the parties adopted rules on an issue, they will start on equal footing when discussing an enforcement strategy that is new to both of them.

Interestingly, officials on both sides of the Atlantic have opined on the best ways to proceed with international securities regulation. According to Tafara, fighting securities violations internationally means maintaining a great deal of trust in a foreign counterpart's competence and discretion:

Specifically, each securities regulator must be able to:

- Collect, under compulsion if necessary, key types of information essential to conducting an investigation, including bank and brokerage records and beneficial ownership information;
- Share non-public information in its files with a foreign counterpart relevant to the investigation the foreign counterpart is conducting;
- Conduct an investigation in its territory on behalf of a foreign counterpart irrespective of whether the conduct in question violates, or would violate, the securities regulator's law;
- Allow information shared with a foreign counterpart to be used to facilitate the foreign counterpart's investigation and resulting proceedings, including assisting in a criminal prosecution; and
- Outside of the permissible uses, maintain the confidentiality of non-public information received from a foreign counterpart.

Tafara Speech, *supra* note 3. This means that a securities regulator should have the ability to use its enforcement powers on behalf of a foreign authority to the same extent as they are used by the securities regulator to enforce compliance with domestic securities laws. *Id.*

The EC's Commissioner McCreevy has laid out his own "Six Principles for Building a Transatlantic Market" which emphasize not only teamwork but also the value of regulatory diversity:

Firstly, the old dictum: **do no harm**. Regulators should attempt to stay out of the line of play as much as possible: to observe closely, to step in when needed, but only to do so when absolutely necessary.

Secondly, we should do so in a **co-ordinated multilateral manner**, rather than attempting to build the foundations of the new order on a thicket of bilateral agreements and understandings.

Third, we should get rid of as much **regulatory duplication** as possible. If another regulator offers an equivalent standard of regulation and equivalent enforcement, have the courage to rely on them!

Fourth, this **equivalence recognition** should be based on global understandings and global standards. The G7 have just called for more free trade in securities based on mutual recognition of regulatory regimes. We will also need to bind in our partners in China, India and others.

Fifth, let **transatlantic markets serve as the laboratory of globalisation**. Financial market integration runs deepest between the EU and the US. This is why we should lead by example and show how regulators, supervisors and legislators can cooperate. If we can't do the job—why should we expect emerging markets to adopt some of our ways?

Sixth and finally, underneath these principles, there need to be **consistent implementation, information sharing and enforcement** at technical level between individual jurisdictions. Enforcement based on the laws of each others [sic] respective jurisdiction—not the octopus tentacles of extraterritoriality.

Let me be clear here: this global regulatory cooperation does not mean creating a regulatory superstate. Regulation does not need to be the same colour in every state. Some regulatory alternatives and competition can be a good thing. The solution to the world's ills is not a global Sarbanes-Oxley!

What we need is open access, compatibility, a sensible balance between investor protection and economic freedom. Investors want choice. We cannot attempt to extinguish all risk: we have to manage it within reasonable limits. Legal systems that attempt to regulate it away fail.

Charlie McCreevy, European Comm'r for Internal Mkt. and Servs., Building the Transatlantic Marketplace, Speech Before the Heyman Center on Corporate Governance 4 (Mar. 7, 2007), *available at* <http://europa.eu/rapid/SearchAction.do> (search complete database, reference "SPEECH/07/131") [hereinafter McCreevy Speech, Building the Transatlantic Marketplace].

But a full explanation of international regulatory cooperation must examine particular incidents of cooperation with three key questions in mind: “why?, about what?, and how?”²⁸ These questions are crucial to explaining when each of the various stages and forms of regulatory cooperation is appropriate. The Organisation for Economic Co-operation and Development (“OECD”) has divided regulatory cooperation into three categories, defined by the stage at which cooperation occurs: “pre-regulatory arrangements,” “regulatory arrangements,” and “post-regulatory arrangements.”²⁹ Agencies naturally begin the regulatory process in a policy development stage, during which pre-regulatory arrangements may help states participate in each other’s rule-making process by, for example, exchanging information relevant to policy design.³⁰ An agency’s next step is to adopt the regulations themselves. Here, a regulatory arrangement may dictate the adoption of common or congruent regulation.³¹ Finally, once a regulation has been adopted it must be enforced.³² Post-regulatory arrangements range from pooling resources into a supranational enforcement authority to arranging for mutual recognition of each party’s enforcement authorities.³³

28. Kalypso Nicolaïdis, *Regulatory Cooperation and Managed Mutual Recognition: Elements of a Strategic Model*, in TRANSATLANTIC REGULATORY COOPERATION: LEGAL PROBLEMS AND POLITICAL PROSPECTS 571, 573 (George A. Bermann, Matthias Herdegen & Peter L. Lindseth eds., 2000).

29. *Id.* at 580–81.

30. *Id.* at 581. According to Kalypso Nicolaïdis:

Coordination at this stage may also serve to establish the ‘equivalence’ of standards in order to facilitate the implementation of agreements over the enforcement of such standards What matters chiefly at this stage, however, is the process of consensus-building and the progressive convergence in regulatory culture that may accompany it, rather than the end result in itself. There is no legally binding consequence to cooperation at this stage but its function is to attempt to coordinate regulatory action so as to increase regulatory effectiveness when addressing cross-border problems.

Id.

31. *Id.* at 581–82. The results at this stage can vary greatly in terms of the degree of their similarity and legally binding effect. The spectrum of possibilities ranges from a binding treaty containing the text of the full regulation to an informal understanding that the parties involved agree on a general approach to a problem. *See id.*

32. *Id.* at 582. Note that

[t]he term ‘enforcement’ is used here not only in the narrow legal sense of intervention by regulatory or judicial authorities in case of breach of law, but in the more general sense of the range of activities necessary to ensure that a given rule is interpreted, applied, and enforced adequately by the parties concerned. Certification, licensing, or approval all refer to this last stage of rule-making.

Id.

33. *Id.* Note also that cooperation can be targeted specifically to a relevant stage in the enforcement process:

Regulatory cooperation varies not only with regard to which phase of regulation it affects, but also in terms of the depth of cooperation. Most generally, cooperation can be divided into hard or soft forms.³⁴ More specifically, though, the means of cooperation can be categorized by the type of delegation used. First, convergence and consensual harmonization can occur without any delegation at all.³⁵ Such a system allows each individual state to enforce its own regulations—which just happen to be equivalent to those of partner states. This form of soft cooperation therefore minimizes the leap of faith required of the states involved but, because it is non-binding, provides no means for ensuring states stick to their harmonized goals. Second, participating states can opt for some sort of hard cooperation, like supranational regulation through vertical delegation. That means, in addition to harmonizing their regulations and enforcement procedures, states can transfer “some degree . . . of competence above the nation-state to entities that, while usually constituted by nation-states, are not entirely controlled by them.”³⁶ Third, the states can follow a path toward mutual recognition, which requires some horizontal delegation of regulatory competence to a foreign sister agency at the same level of governance.³⁷ Last, the states can regulate

[Cooperation in enforcement] can be aimed at the *input* level of enforcement (data gathering and analysis), at the *determination* level of enforcement (establishing whether the product or the service is to be considered lawful), or at the final *outcome* stage (issuing stamps of approval or certificates of conformity, thus having a direct effect on market access).

Id.

34. International regulatory cooperation takes many shapes. In the securities regulation field, these include “1) hard international rules that constrain financial institutions . . . ; 2) softer principles of supervision that bureaucrats [in other countries may emulate;] and 3) models for regulators in adjacent issue areas.” David Zaring, *Informal Procedure, Hard and Soft, in International Administration*, 5 CHI. J. INT’L L. 547, 548–49 (2005).

35. Nicolaïdis, *supra* note 28, at 585.

This form of regulatory cooperation relies simply on direct collaboration between regulators of different countries, acting through a range of methods ranging from simple exchange of information, to exchange of scientific data relevant to regulatory decision-making, to the actual adoption of similar regulations. Such adoption could even occur through a formalized process of negotiation, but this would have to be by consensus and without binding effects justifying supranational dispute settlement.

Id.

36. *Id.* at 586.

37. *Id.*

Regulators can recognize other countries’ regulation as equivalent, or at least recognize the enforcement capacity of other countries as equivalent, and delegate this function to them. Private professional bodies can agree to register professionals whose rights of practice have been recognized in another country. Accreditation bodies can accept the stamps of approval granted to laboratories or universities by their peers in other countries. Horizontal delegation, like vertical delegation, usually involves a degree of sharing of tasks and responsibilities, but

through a system of managed mutual recognition, which combines both horizontal and vertical delegation. This kind of cooperation is a sort of compromise between the two previous types, in that it captures the positive elements of horizontal delegation (a less “drawn-out” process for reaching agreement on the substance and enforcement of the regulations than for vertical delegation)³⁸ while using elements of vertical delegation (like “the creation of common minimal rules and a dispute-settlement mechanism to manage potential disagreements” between states) to prevent regulatory competition.³⁹

These two elements of international regulatory cooperation—the stage and type—are highly intertwined. In fact, certain stages of the regulatory process are more amenable to particular means of cooperation. To a certain extent, the stage of regulation often dictates the types of cooperation available (and vice versa).⁴⁰ As Kalypso Nicolaïdis has described, when states seek to enter into pre-regulatory arrangements at the policy development stage, their efforts will usually result in consensus, rather than delegation.⁴¹ Conversely, she adds, if states choose to cooperate at the policy adoption stage, both horizontal and vertical delegation may be necessary in order to ensure desired results.⁴² At the enforcement stage, moreover, vertical delegation is unlikely since “[s]uch missions [supranational competition agencies and accreditation laboratories, for example,] are much more resource-intensive and sensitive

only qualifies as such if some degree of competence falls completely outside the purview of national regulators.

Id.

38. *Id.* at 594.

39. *Id.* at 587. Due to these benefits, Nicolaïdis believes that this last option will become the paradigm for international regulatory cooperation in the future. *Id.* at 593. Further, Nicolaïdis points out that a “race to the bottom” may result from a system based purely on mutual recognition if a home country favors its nationals and other countries are forced to recognize regulatory decisions made in light of this favoritism. “But,” she notes, “in fact we rarely observe ‘pure’ mutual recognition. Instead, the management of recognition is the trick that regulators have found to satisfy their political masters and trade colleagues while at the same time minimizing the effects of recognition in terms of regulatory competition.” *Id.* at 594.

40. While one element does not necessarily predetermine the other, it does seem that certain combinations of kinds and stages of cooperation result in fewer unnecessary expenditures of effort and sacrifices of autonomy for the parties involved. *Id.* at 590–94.

41. *Id.* at 590.

42. *Id.*

The experience of the European Union seems to have shown that at the adoption stage, horizontal delegation alone (e.g., pure mutual recognition) is generally not feasible without prior convergence-based cooperation. More to the point, we usually observe some level of vertical delegation alongside horizontal delegation, to the extent that the binding character of the recognition needs to be enforced by dispute-settlement bodies.

Id.

than the creation of international standards per se and carrying them through most often involves a physical control and presence rendering delegation much more tangible.”⁴³

In sum, successful international regulatory cooperation does not mean the same thing in every context. In other words, the goal of international regulatory cooperation is not necessarily to create a single international regulatory code any more than it is to create a supranational body to enforce this code. To maximize efficiency, cooperation should be pinpointed to the relevant aspects of the regulatory apparatus, both in terms of when and how the cooperation takes place.

III. CHECKING OUT OF HOTEL CALIFORNIA TOGETHER: COOPERATION BETWEEN THE UNITED STATES AND EUROPEAN UNION ON FOREIGN COMPANY DEREGISTRATION FROM U.S. MARKETS

A. *Deregistration Requirements, Sarbanes-Oxley, and Hotel California*

This Note begins its examination of regulatory cooperation between the United States and EU with the recent changes in SEC regulations regarding the deregistration of foreign issuers. The deregistration regulation in question⁴⁴ had been on the books for forty years until SOX altered the regulatory landscape and made deregistration a tempting proposition for many foreign companies.⁴⁵ One can barely overstate the impact of SOX on securities markets.⁴⁶ The Act shocked the system of

43. *Id.* at 590–91. States often prefer to cooperate in the policy development stage because it does not usually involve the kind of leap of faith necessary to carry out a system of delegation. Nicolaïdis points out that, in the context of trade regulation, “experience with the conduct of these negotiations has shown that regulatory cooperation over enforcement or approval is much more sensitive than trade negotiators initially assumed.” *Id.* at 589. Indeed, one of the recommendations most commonly advanced in Commission circles for promoting transatlantic regulatory cooperation is that parties start their discussions early on in the regulatory process, when they will be less likely to have already committed themselves to a regulatory position. *Id.* Perhaps ironically, when states do not begin their cooperation until later stages of regulation, they are apparently often working on the assumption that it is easier to subcontract enforcement activities like testing or licensing than to “harmonize or mutually recognize regulations that reflect deep-seated historical, institutional and cultural differences between countries.” *Id.* But Nicolaïdis retorts that even enforcement actions are fraught with conflicts—for example cultural attitudes about the level of tolerable risk or economic conditions affecting the political flack a government will receive for taking adverse enforcement action on a company may differ significantly from one country to another. In any case, cooperation at any level may ultimately lead to cooperation at other levels of the regulatory process. *Id.* at 590–91.

44. Rule 12d2-2 of the Securities Exchange Act of 1934, Removal from Listing and Registration, 28 Fed. Reg. 1506 (Feb. 16, 1963) (current version at 17 C.F.R. § 240.12d2-2 (2008)).

45. *EU/US: US-Listed Firms Escape Hotel California*, EUROPEAN REP., Feb. 15, 2007 [hereinafter *US-Listed Firms Escape Hotel California*].

46. Then-SEC Commissioner Paul S. Atkins called SOX a “corporate governance equivalent of

securities issuers because it not only brought about great substantive changes in securities and corporate governance laws, but it did so at breakneck speed in reaction to Enron and other corporate scandals.⁴⁷ Almost immediately, SOX faced staunch criticism from overseas.⁴⁸

This criticism stemmed from various provisions with which foreign firms may have difficulty complying. For example, SOX mandates that a company's CEO and CFO personally certify, on pain of civil damages, that financial statements do not contain any material misstatements or omissions and that the corporation has internal controls designed to generate complete and accurate financial information.⁴⁹ It also mandates a specific relationship between a company and its management⁵⁰ and places "particularly intrusive requirements" on the audit process.⁵¹

the 'shot heard round the world.' With the implementation of Sarbanes-Oxley . . . the U.S. government has completed the largest financial services regulatory initiative since the regulatory initiative from which the SEC was born." Paul S. Atkins, Comm'r, Sec. & Exch. Comm'n, Remarks Before the European Institute of the University of Gent (Jun. 23, 2005), *available at* <http://www.sec.gov/news/speech/spch062305psa.htm> [hereinafter Atkins Speech, University of Gent].

47. Oddly enough, a bipartisan effort transformed this almost unprecedented change in securities regulation from a mere proposal to enacted legislation in just seven months after Enron filed for bankruptcy. John Paul Lucci, *Enron—The Bankruptcy Heard Around the World and the International Ricochet of Sarbanes-Oxley*, 67 ALB. L. REV. 211, 215 (2003). Even Commissioner Atkins admits that "[t]he pace of this new wave of regulation has been daunting for U.S. and non-U.S. companies alike" Atkins Speech, University of Gent, *supra* note 46.

48. John Paul Lucci explains the typical reaction to SOX from around the globe:

While many in the United States heralded the Act as ushering in "a 'new era of corporate accountability and responsibility,'" it received a less receptive welcome overseas. Almost from the beginning, foreign commentators criticized Sarbanes-Oxley as a hastily drafted, quick-fix to corporate governance problems. One British financial reporter observed that "[i]n reality . . . [the Act] is a pre-election political compromise meant to give US voters the impression that Congress and the White House are getting tough on those issuing fraudulent account[s]—but the markets are not looking significantly better." Similarly, a South African journalist commented that "[t]he instant response of legislators to any crisis is to pass laws."

Lucci, *supra* note 47, at 217 (footnotes omitted).

49. Robert C. Pozen, Can European Companies Escape U.S. Listings? 2 (Harvard Univ., John M. Olin Ctr. for Law, Econ., & Bus., Discussion Paper No. 464, 2004), *available at* http://www.law.harvard.edu/programs/olin_center/papers/464_pozen.php (click on "464:PDF" hyperlink). *See also* Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745, § 302(a), 15 U.S.C. § 7241 (2006).

50. Pozen, *supra* note 49, at 2. This relationship includes a prohibition on almost all loans from the company to its officers and directors and requires repayment by senior officials of certain bonuses and trading profits following any accounting restatements "resulting from misconduct." *Id.*; Sarbanes-Oxley Act, § 304.

51. Pozen, *supra* note 49, at 2. Specifically, the audit committee must consist of only independent directors, with some exceptions to accommodate home country laws, and any foreign firm auditing a foreign listed company must submit itself for U.S. inspection. *Id.*; Sarbanes-Oxley Act, §§ 301, 106. Additionally, SOX also established an entire non-profit organization, the PCAOB, "to oversee the audit of public companies that are subject to the securities laws, and related matters." Sarbanes-Oxley Act § 101(a). Its duties include registering public accounting firms; "establish[ing] or adopt[ing], or both, by rule, auditing, quality control, ethics, independence, and other standards relating to the preparation of audit reports for issuers"; conducting inspections of and disciplinary

In some cases, compliance with provisions like these is unduly duplicative of a home country's procedures or even outright illegal according to home country law. For example, France has already created two independent institutes to oversee accounting firms.⁵² Thus, those studying French markets wonder "why it is necessary for French companies to follow the regulations of Sarbanes-Oxley's PCAOB [Public Company Accounting Oversight Board] when [France] already has two of its own oversight boards."⁵³ The Act's rules also conflict with the general corporate framework in Germany, where there is no chief executive to certify financial statements and where board composition generally does not allow for independent audit committees.⁵⁴ Moreover, compliance with SOX would constitute an outright violation of Australia's corporations law, which gives shareholders the "final say" in auditor selection.⁵⁵

Whether they are motivated by the need to comply with conflicting home country rules, or merely by a desire to avoid the added costs of SOX compliance,⁵⁶ foreign firms could often not avoid the Act. Because SOX

proceedings concerning registered accounting firms, including imposing sanctions when justified; and generally enforcing compliance with SOX. *Id.*

52. These are the *Ordre des Experts-Comptables* (National Institute for Chartered Accountants) and the *Compagnie Nationale des Commissaires aux Comptes* (National Institute for Statutory Auditors). Lucci, *supra* note 47, at 240 (citing *France: Turmoil for Some, Opportunity for Others*, INT'L. ACCT. BULL., Nov. 12, 2002 at 10, 2002 WL 11544700.)

53. *Id.*

54. *Id.* at 243. In Germany, "[t]he board's leader—the *Sprecher*—has no legally defined role and half of the supervisory board, which performs audit functions, is composed of employees and union representatives who are, by definition, not independent." *Id.* *But see* Atkins Speech, University of Gent, *supra* note 46 ("Broadly speaking, Sarbanes-Oxley reflects goals shared by Europeans and Americans with respect to strengthening corporate governance. Sarbanes-Oxley's promotion of independent audit committees, for example, confirmed a global trend toward setting up such audit committees.").

55. Lucci, *supra* note 47, at 243 (quoting Mark Fenton-Jones, *Warning on US Law for Local Groups*, AUSTL. FIN. REV., Oct. 25, 2002, at 58, 2002 WL 87784).

56. European complaints about the costs of compliance are more than just the grumblings of those unwilling to see the status quo change. Even SEC Commissioner Atkins admitted frankly that the costs of compliance were much higher than expected:

But it is indisputable that everyone greatly underestimated the costs involved in the [SOX §] 404 process. When the SEC first released its implementation rules for 404, we estimated that the aggregate costs of the rule would be about \$1.24 billion or \$94,000 per public company. In the SEC's defense, we made this estimate before the PCAOB released its 300 page Auditing Standard No. 2. Unfortunately, surveys indicated that actual costs incurred for 404 compliance were TWENTY times higher than what we estimated. Many had predicted last year that almost half of the costs incurred to comply with Section 404 were first-time start up costs that would not be repeated in year 2. A recent study that was sponsored by the Big 4 Accounting Firms predicted that total 404 implementation costs would decline in year two, but the biggest cause of the decline was expected to be reduced documentation costs for the companies. But, [sic] I would be surprised if companies' out-of-pocket costs or auditors' 404 revenues will fall.

applies to all companies required to register with the SEC,⁵⁷ the only way for foreign companies to escape it is to delist from U.S. exchanges and then deregister with the SEC.⁵⁸ Yet this was often much easier said than done because, until recently, a foreign company with more than three hundred U.S. shareholders could not deregister.⁵⁹

Paul S. Atkins, Comm'r, Sec. & Exch. Comm'n, Remarks Before the Securities Regulation Institute, San Diego, Cal. (Jan. 19, 2006), available at <http://www.sec.gov/news/speech/spch011906psa.htm>.

57. As defined in the Act:

[T]he term "issuer" means an issuer (as defined in section 3 of the Securities Exchange Act of 1934 . . .), the securities of which are registered under section 12 of that Act . . . , or that is required to file reports under section 15(d) . . . , or that files or has filed a registration statement that has not yet become effective under the Securities Act of 1933 . . . , and that it has not withdrawn.

Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745, § 2 (a)(7), 15 U.S.C. 7201 (2006). Note that this definition makes no distinction between foreign and domestic issuers. See also Peter Hostak et al., *An Examination of the Impact of the Sarbanes-Oxley Act on the Attractiveness of US Capital Markets for Foreign Firms*, 5 n.4 (2007), available at <http://ssrn.com/abstract=956020> (citing SEC Release Nos. 33-8124 and 33-8177 as examples of the SEC's confirmation that SOX provisions apply equally to foreign firms, in part because the purpose of SOX is "to restore investor confidence in U.S. financial markets, regardless of the origin of the market participants"). Note further that "[t]he word 'foreign' appears 18 times in the Sarbanes-Oxley Act and none of these mentions exemptions or distinctions between the requirements for domestic firms vs. foreign firms." *Id.*

58. Delisting and deregistration are actually two separate processes. "Delisting" is specific to a particular exchange and does not in and of itself excuse a firm from SEC reporting requirements. A company seeking to delist from an exchange must follow that particular exchange's rules for delisting and then make its intentions known to the SEC on Form 25. "Deregistration," on the other hand, follows delisting and will free the party from all SEC filing requirements. Peter Hostak et al. describe the process as follows:

[F]or example, in the case of NYSE, the company submits a letter indicating its intention to delist and a board resolution approving the delisting. The SEC can then impose additional terms if necessary to protect investors, but has not done so for many years. The delisting can become effective after 10 days from the filing date. The delisting is typically followed by deregistration."

Id. at 6 (footnote omitted). See Section 12(d) of the Securities Exchange Act of 1934, 15 U.S.C. § 781 (2006), for further information.

59. *US-Listed Firms Escape Hotel California*, *supra* note 45. Of course, a company wishing to deregister can try to reduce the number of its U.S. shareholders:

Some of the options that are available to foreign companies to reduce the number of US shareholders are reverse stock splits, adjustments of the exchange ratio on the ADR program, amendment of articles to seize minority shareholdings, share buybacks, and reduction of capital. However, these measures cannot be targeted exclusively to US investors. Some of them require court or shareholder approvals and risk bad publicity for the firm due to their adversity to minority shareholders. Therefore, deregistration is likely to be a time consuming and costly procedure.

Hostak et al., *supra* note 57, at 7 (citation omitted). In any case, the three hundred shareholder threshold for deregistration is somewhat of an oversimplification because, at the time SOX became law, more rigorous requirements existed for companies issuing American Depositary Receipts ("ADRs"). A company that trades through ADRs basically gives U.S. investors the ADR as a stand-in for stock issued in its home country; a depository institution acts as custodian for the ADR and can cash in ADRs for the foreign stock (or cash equivalent) if the foreign firm decides to stop trading in the United States. The SEC classifies ADRs into three levels and subjects Level II and III ADRs to its

The limitations on deregistration turned U.S. securities markets into what some referred to as the “Hotel California.”⁶⁰ But the complaints were not limited to a few spurned corporations. In fact, many market watchers opined that the Hotel California situation had trapped more than foreign companies attempting to delist—it also scared growing foreign companies away from listing with U.S. markets in the first place.⁶¹ Even the EC

reporting requirements. *Id.* at 4–5. Some foreign firms trading in the United States through ADRs had a particularly difficult time opting out of SOX reporting requirements:

[T]he difficulty of complying with the “fewer than 300 US shareholders” requirement [was] exacerbated by continuing requirements that the number of US shareholders stays below 300 permanently for Level III ADRs and for at least 18 months for Level II ADRs. Otherwise, the company’s reporting obligations resume. Since some foreign firms may have more than 300 US shareholders outside their ADR programs or some investors may buy shares to hold up the firm’s delisting, the termination of ADR programs alone need not be, by itself, sufficient for foreign firms to deregister from the SEC.

Id. at 6–7.

60. As one commentator put it, “you can check out but you can never leave.” *US-Listed Firms Escape Hotel California*, *supra* note 45. The frustration of foreign companies and market commentators apparently manifested itself in the creation of clever nicknames. SEC Commissioner Atkins described the deregistration situation as a “roach motel.” Paul S. Atkins, Comm’r, Sec. & Exch. Comm’n, Speech by SEC Commissioner: Remarks at Finance Dublin (Mar. 26, 2007), available at <http://www.sec.gov/news/speech/2007/spch032607psa.htm> [hereinafter Atkins Speech, Dublin].

61. SEC Commissioner Atkins espoused this view:

Foreign issuers found it difficult to meet [the standard for deregistration in place at the passage of SOX] even if there was relatively little investor interest in the United States. Thus, there was a widespread perception that a decision to list in the U.S. could never be reversed—the aptly named “roach motel.” This perception, in turn, serves as a disincentive to list securities in the U.S. in the first place.

Id. Many market watchers and scholars have taken the opinion that SOX draws business away from U.S. markets in general. *See also* Lucci, *supra* note 47, at 237 n.188 (pointing to the chairman of the London Stock Exchange’s statement that “Sarbanes-Oxley will make American markets ‘far less attractive and welcoming to foreign issuers’” (citing *LSE Head Attacks US Law*, *TIMES* (London), Dec. 10, 2002, at 21)). Moreover, the New York Stock Exchange responded to business leaving the United States as a result of SOX by merging with the European exchange Euronext. The resulting transatlantic exchange, NYSE Euronext, has given “‘an absolute assurance’ that U.S.-style regulation would not spread to Europe as a result of the merger.” James Kanter, *Asia Is Next on List for Exchanges’ Expansion; Newly Merged NYSE Euronext Has Asian Ambitions*, *INT’L HERALD TRIB.*, Apr. 4, 2007, at 10. Not everyone agrees with this conclusion, however. For example, Hostak et al. performed empirical research showing that the cost of compliance with SOX was not a main reason for recent delistings:

Our results indicate that delisting firms had corporate governance characteristics that are generally deemed to be poor compared to those of foreign firms that decided not to delist (e.g., lower percentage of independent directors, smaller boards, higher CEO ownership, and lower financial reporting quality). Further, we document that relative to the stock prices of foreign firms with “better governance,” the share prices of firms with bad governance characteristics fell less when SOX was passed, consistent with our hypothesis that investors believed that SOX is likely to reduce [managers and controlling shareholders’] exploitation of non-controlling investors.

claimed that the “asymmetric” restrictions on European companies’ ability to leave U.S. markets would endanger European and American markets.⁶² Given the complaints stemming from both sides of the Atlantic, the SEC’s revision of its deregistration rules was prime fodder for regulatory cooperation between the United States and EU.⁶³

B. The SEC Incorporates the EC’s Feedback into Its Revised Deregistration Rule

Throughout this deregistration (mini-)crisis, the SEC and EC worked together to develop a policy in the interest of the transatlantic market as a whole. This cooperation consisted mainly of low-commitment, low-

Moreover, our analysis of the stock price reaction at the delisting announcement date documents a negative stock-price response. This result implies that investors were disappointed that the firms avoided the corporate governance improvements required by SOX

Hostak, et al., *supra* note 57, at 2.

In fact, many of those who claim SOX has been bad for U.S. markets seem to be seeing the issue through the frame of transatlantic financial markets. The trend of Chinese companies flocking to U.S. markets after SOX remains largely unexamined, even though “China could soon become Nasdaq’s biggest source of non-U.S. listings” Joe McDonald, *Nasdaq Says Chinese Listings Growing*, READING EAGLE, Aug. 9, 2007, available at <http://readingeagle.com/article.aspx?id=54034>. In fact, as of the fall of 2007, Chinese companies seemed undeterred by the recent sub-prime mortgage crisis in the United States, rather Chinese companies were coming to the United States to gain visibility and legitimacy. According to former Representative Michael Oxley, one of SOX’s namesakes (who coincidentally now works for Nasdaq Stock Market Inc.), SOX has actually attracted Chinese companies to U.S. markets:

It’s a combination of accessing the most liquid and visible market in the world and, I guess you could call it, the prestige of listing with a market that has such high standards

I think they [Chinese companies] aspire to play in the big leagues, and they know they have to meet these requirements to do so So instead of whining or backing off, they have made a determination that this is a competitive advantage to them in the marketplace to say they have made a decision to meet these higher standards.

Id.

62. The DG Markt noted in its comments on proposed changes to the deregistration rules:

We believe both Europe and the United States will benefit from more open and competitive markets, where European issuers are not kept in an asymmetric situation of being able to enter U.S. capital markets but virtually unable to exit them, whereas U.S. issuers do not encounter the same difficulties in the EU.

Letter from D.J. Wright, on Behalf of Alexander Schaub, Dir. Gen. Internal Mkt. & Servs., European Comm’n, to Nancy Morris, Sec’y, Sec. & Exch. Comm’n (Mar. 1, 2006), available at <http://www.sec.gov/rules/proposed/s71205/ec010306.pdf>.

63. The term “international regulatory cooperation” usually conjures up images of parties working together to create a common regulatory standard or enforcement procedure. Its use might thus seem out of place in a situation like this, in which only one country is changing its rules. Yet, securities regulation is aimed at the securities market as a whole, so to the extent that any changes made to U.S. deregistration rules will affect the big picture of transatlantic securities regulation, these changes are an integral part of the effort toward transatlantic regulatory cooperation.

intensity acts like sharing information and opinions relevant to drafting the rule. Yet without further explanation, this technical description dismisses the close contact between the two sides and misrepresents a process that led to what both parties found to be a favorable result.

As it turned out, checking out of Hotel California was not as easy as simply lowering the threshold of U.S. shareholders allowed for deregistration. In fact, the SEC's first proposal,⁶⁴ which to a great extent did just that, was a flop. This proposal was based on a "public float" test, meaning that the SEC essentially transformed the fixed, three hundred-share test into a proportional test allowing foreign companies to deregister if their U.S. shareholders held less than a certain percentage of their total worldwide public float.⁶⁵

64. Removal from Listing and Registration of Securities Pursuant to Section 12(d) of the Securities Exchange Act of 1934, 70 Fed. Reg. 42,456 (proposed Jul. 22, 2005) (to be codified at 17 C.F.R. pts. 232, 240, 249) [hereinafter First Deregistration Proposal]. In its second version of the proposal, the SEC noted its motivation stemmed from many of the issues discussed above:

The Commission proposed to amend these rules out of concern that, due to the increased globalization of securities markets in recent decades as well as other trends, it has become difficult for a foreign private issuer to exit the Exchange Act reporting system even when there is relatively little U.S. investor interest in its U.S.-registered securities.

We recognize that U.S. investors benefit from the investment opportunities provided by foreign private issuers registering their securities with the Commission and listing and publicly offering those securities in the United States. However, because of the burdens and uncertainties associated with terminating registration and reporting under the Exchange Act, the current exit process may serve as a disincentive to foreign private issuers accessing the U.S. public capital markets.

Termination of a Foreign Private Issuer's Registration of a Class of Securities Under Section 12(g) and Duty to File Reports Under Section 13(a) or 15(d) of the Securities Exchange Act of 1934, 72 Fed. Reg. 16,934, 16,934-35 (proposed Apr. 5, 2007) (to be codified at 17 C.F.R. pts. 200, 232, 240 & 249) (footnotes omitted) [hereinafter Second Deregistration Proposal].

Alternatively, SEC Commissioner Roel C. Campos provides a much more incisive account of the reason for the revision:

The bottom line is that we in the U.S. should be confident enough in the competitiveness of our markets to allow companies to exit our reporting regime when there is relatively little U.S. interest in the securities of those companies. If there is enough U.S. investor interest, these companies will stay. If not, they should be free to go. It seems to me that part of making our markets as attractive as possible to foreign issuers, is removing the concern that once in the U.S. markets, a company would be stuck there.

Roel C. Campos, Comm'r, Sec. & Exch. Comm'n, Remarks at the Open Meeting: Foreign Private Issuer Deregistration (Dec. 13, 2006), available at <http://sec.gov/news/speech/2006/spch121306rcc3.htm>.

65. Second Deregistration Proposal, *supra* note 64, at 16,935. The proposed standard distinguished between issuers that qualify as well-known seasoned issuers ("WKSIs") and non-WKSIs:

Under the original rule proposal, a WKSI would have been eligible to terminate its Exchange Act reporting obligations regarding a class of equity securities if the U.S. average daily trading volume ("ADTV") of the subject class of securities had been no greater than 5 percent of the ADTV of that class of securities in its primary trading market during a recent

The SEC received many comments criticizing the proposal.⁶⁶ Notably, the EC made its feelings clear through many public speeches and even an official comment letter filed with the SEC. The comment letter clearly shows a great deal of effort and dedication on the part of EU officials to influence U.S. securities regulation. Indeed, the eleven-page letter provides a statistical analysis of the SEC's proposal that reads almost like a white paper the EC would have prepared for DG Markt's own policymaking.⁶⁷ It even includes a policy suggestion that the new threshold be set much higher—at three thousand U.S. shareholders or “preferably higher.”⁶⁸ To hammer its position home, European Commissioner for Internal Market and Services, Charlie McCreevy, mentioned the shortcomings of the original proposal in several public speeches to American audiences in just over a year; in these speeches he vowed to help the SEC formulate rules that would allow more EU firms to deregister.⁶⁹

Perhaps the most telling sign of cooperation here is that the SEC and EC held a video teleconference to discuss “some of the issues raised in the European Commission's comment letter on the Commission's proposed rules relating to foreign issuer deregistration.”⁷⁰ Although there is no

12 month period, and U.S. residents held no more than 10 percent of the issuer's worldwide public float as of a specified date. A WKSII with greater than 5 percent U.S. ADTV or a non-WKSII would have been eligible for termination of reporting regarding a class of equity securities if, regardless of U.S. trading volume, U.S. residents held no more than 5 percent of the issuer's worldwide public float as of a specified date.

Id.

66. The SEC received more than fifty comment letters on the proposal, many from European companies criticizing the public float test. In addition to the predictable requests for liberalizing the deregistration rules by raising the percentage of U.S. shareholders allowed, some comments suggested excluding certain types of investors from the calculation of U.S. shareholders. Paul S. Atkins, Comm'r, Sec. & Exch. Comm'n, Remarks Before the Institute of European Affairs, Dublin, Ir. (Sept. 29, 2006), available at <http://www.sec.gov/news/speech/2006/spch092906psa.htm>. *But see* Second Deregistration Proposal, *supra* note 64, at 16,935 (stating that the SEC only received thirty comment letters which “represented the views of over 40 distinct entities”).

67. For example, the EC letter informs the SEC that of the approximately seventy issuers incorporated in the EU Member States with the greatest market capitalization and presence in U.S. markets, only about six or seven would be able to deregister under the proposal—about fifteen percent fewer than the SEC predicted. In any case, it continues, even the SEC's predicted twenty-six percent of foreign private issuers eligible to deregister is not ambitious enough, considering that no EU Member State has similar restrictions on deregistration. Letter from D. J. Wright, *supra* note 62, at 2–3.

68. *Id.* at 8.

69. *See, e.g.*, McCreevy Speech, U.S. Chamber, *supra* note 2; Charlie McCreevy, European Comm'r for Internal Mkt. & Servs., The Transatlantic Capital Market—Fulfilling Its True Potential, Speech Before the US Chamber of Commerce 4 (Feb. 8, 2006), available at <http://europa.eu/rapid/SearchAction.do> (search complete database, reference “SPEECH/06/64”); McCreevy Speech, Building the Transatlantic Marketplace, *supra* note 27, at 2.

70. Memorandum from Paul Dudek, Chief, Office of Int'l Corporate Fin., Div. of Corp. Fin.,

further description of the discussions at the meeting, the confidential, non-public nature of the meeting and the high level of officials attending imply that the meeting was held to work seriously together through substantive policy issues.⁷¹

With this input in mind, the SEC issued a revised proposal for the deregistration rule.⁷² The second proposal abandoned the public float test for a test based on average daily trading volume. Instead of relying on the location of shareholders themselves, this new test compares a firm's average daily trading volume in the United States with its worldwide average daily trading volume, setting a five percent threshold for deregistration.⁷³

As before, the EC submitted a formal comment letter in response to the second proposal. This time, however, it used the letter as an opportunity to express its approval of the revised proposal, saying it "takes proper account of all stakeholders' interests and sets domestic concerns in the wider, global picture."⁷⁴ The Commission also issued a press release in which Commissioner McCreevy showered praise on the new rule and on the transatlantic regulatory dialog that helped create it.⁷⁵

C. EVALUATING THE COOPERATION BETWEEN THE UNITED STATES AND EU ON THE SEC'S DEREGISTRATION RULES

The cooperation between the EC and SEC resembles the kind of low-intensity, low-commitment cooperation that commentators have said is

Sec. & Exch. Comm'n, to File No. S7-12-05 (Jul. 24, 2006), *available at* <http://www.sec.gov/rules/proposed/s71205/s71205-58.pdf>.

71. The high-profile (by securities regulation standards) participants included no less than, on the European side, the Director of Financial Markets of the EC and the First Secretary of the EC's delegation in Washington, D.C., and, on the American side, the Director of the SEC's Division of Corporate Finance, the Chief of the Division of Corporate Finance's Office of International Corporate Finance, and the Director of the SEC's Office of International Affairs. *Id.* Unfortunately, the only information available to the public about this meeting seems to be a three sentence memorandum included on the SEC's website with the comments on the first deregistration proposal.

72. Second Deregistration Proposal, *supra* note 64.

73. *Id.* at 16,934.

74. Letter from Jörgen Holmquist, Dir.-Gen. for Internal Mkt. and Servs., European Comm'n, to Nancy M. Morris, Sec'y, Sec. & Exch. Comm'n (Feb. 12, 2007), *available at* <http://www.sec.gov/rules/proposed/s71205/s71205-80.pdf>. The EC did, however, make some minor suggestions, including increasing the threshold to allow more foreign companies to deregister. *Id.* at 3.

75. "The SEC's new approach is sensible, practical and workable. . . . This represents real progress, and shows that the EU-US Financial Markets Regulatory Dialogue can make a difference in addressing transatlantic financial issues." Press Release, Delegation of the European Commission to the USA, European Commission Welcomes New US Proposals Allowing Deregistration from Capital Markets (Feb. 14, 2007), *available at* <http://www.eurunion.org/News/press/2007/2007012.htm>.

likely to succeed. None of the EC's comments were required by treaty or other legal obligation. Rather, the parties' motivation stemmed from the merits of the issue and a desire to set up "more open and competitive markets"⁷⁶ (not to mention their interest in representing constituent businesses whose stock is traded in U.S. markets). The intensity of cooperation was also low in the sense that no joint studies or committees were formed—each party came to the table with its own, individually prepared policy research, and the SEC ceded no decisionmaking authority to the EC or any other body. Further, the cooperation was limited solely to the policy development and adoption stages at the SEC—the parties neither called for the EU to adopt a similar rule nor did they seek to create a joint enforcement effort.

Nevertheless, given that the SEC put the second proposed rule into force and the EC voiced its approval of this proposal in its second comment letter, both sides seem content with the result. This situation thus appears to confirm the theory that total, lock-step cooperation does not necessarily mean better cooperation. In fact, informal, low-intensity, or low-commitment regulatory cooperation, or even cooperation limited to a particular stage of the regulatory process, may be all that is necessary to achieve the desired result, especially for a discrete issue like deregistration rules.⁷⁷

IV. DIVERGENT ACCOUNTING STANDARDS

A. *Accounting Standards in the United States and EU*

The passage of SOX put the spotlight on the costs a company faces when it allows its securities to be traded in foreign markets. As mentioned above, foreign companies' complaints about SOX stemmed partly from the sudden increase in compliance costs, especially those costs related to auditing. But these are not the only costs associated with doing business abroad. One of the main problems faced by companies conducting business across the Atlantic is the burden of creating a special financial statement for foreign authorities. The duplication of financial reports results from the different accounting methods required in the United States and EU. These divergent accounting standards are a "leading, and most

76. Letter from D. J. Wright, *supra* note 62, at 2.

77. In this case, requiring total cooperation would mean, among other things, joint enforcement of registration rules. Such a solution is administrative overkill because it would mean cooperation on an essentially domestic issue—the EC would be determining who should or should not be registered with the SEC, and vice versa.

intractable,” hindrance for U.S. companies seeking access to European securities markets, and vice versa.⁷⁸ Just as with deregistration rules, since the SEC and EC believe their interests are best served by working together to open their markets, the two groups are working together to reduce the burden on foreign companies resulting from divergent accounting standards.

Traditionally, the accounting standard in the United States has been the U.S. GAAP.⁷⁹ The EU, on the other hand, has recently implemented the International Financial Reporting Standards (“IFRS”), a unified international standard, in order to help build an integrated market within the Union and to move toward proposed international accounting standards.⁸⁰ The variations in these two accounting standards mean that if foreign companies do not wish to pay for two different sets of financial statements, their only option is to make exceedingly complicated reconciliations to provide information in the form required by the other accounting standard.⁸¹

B. Cooperation on Accounting Standards: Convergence, Not Equivalence

The accounting standards problem is complicated by the fact that accounting standards have evolved over a long period of time and have become deeply entrenched in their respective countries. The problem is thus somewhat more complicated than the deregistration issue because

78. Joel P. Trachtman, *Transatlantic Regulatory Cooperation from a Trade Perspective: A Case Study in Accounting Standards*, in TRANSATLANTIC REGULATORY COOPERATION, *supra* note 28, at 223, 224.

79. *Id.* at 228.

80. McCreedy Speech, U.S. Chamber, *supra* note 2, at 2. The IFRS is the brainchild of the International Accounting Standards Committee (“IASC”) and its successor, the International Accounting Standards Board (“IASB”), the international accounting standard-setting body, which bore the responsibility of developing “a core set of accounting standards that could serve as a framework for financial reporting in cross-border offerings.” Concept Release on Allowing U.S. Issuers to Prepare Financial Statements in Accordance with International Financial Reporting Standards, 72 Fed. Reg. 45,600, 45,600-01 (Aug. 14, 2007). Almost one hundred countries either require or accept financial statements prepared using IFRS standards. In 2005, the EU began requiring companies incorporated in Member States and whose securities are listed on EU markets to file their financial reports on an endorsed IFRS. *Id.* at 45,602.

81. For example, if a foreign issuer does not want to file financials compiled according to U.S. GAAP, it must reconcile its financial statements to U.S. GAAP and “the SEC’s master accounting regulation,” Regulation S-X:

Such reconciliation requires that significant line items such as net income and earnings per share be analysed to show what they would be if US GAAP were applied. The most complete level of reconciliation requires a level of work that approaches the complete conversion of the financial statements to US GAAP.

Trachtman, *supra* note 78, at 228.

whole business cultures have developed around the current accounting standards. But the SEC and EC have several options for resolving the problem. The spectrum of possible solutions ranges from national treatment moderated by a few “ad hoc findings of equivalence and progressive unilateral liberalization,” to mutual recognition, to harmonizing standards to the point of uniformity, to outright inaction.⁸²

Under the circumstances, adopting a uniform standard is impractical at this point because of “differing cultures, business practices, and—most importantly—legal and tort systems.”⁸³ Similarly, given the amount of company resources wasted as a result of reconciliation requirements, inaction is not an option. By process of elimination, then, some form of convergence is the best possibility, and as a result of the 2002 Norwalk Agreement, the organizations responsible for setting U.S. and EU accounting standards are committed to “employ ‘best efforts’ to achieve convergence.”⁸⁴ In other words, the SEC and EC are working to create a reporting system that would allow foreign issuers to file IFRS financial statements in the United States and U.S. GAAP financial statements in the EU with minimal reconciliation. The EC and SEC have therefore chosen to aim for what Commissioner Paul S. Atkins describes as “compatibility, not wholesale uniformity. The goal is not identical results, but rather close alignment and comparable results.”⁸⁵

To these ends, the SEC has established a Work Plan with the EC’s Committee of European Securities Regulators (“CESR”)⁸⁶ which structures their joint work to create “operational and supervisory

82. *Id.* at 224, 239–40.

83. Atkins Speech, University of Gent, *supra* note 46, at 7. Note, however, that the “long-term strategic priority” of the Financial Accounting Standards Boards, the American standard-setting body, and the IASB is to create “a common set of high quality global standards.” Concept Release, *supra* note 80, at 45,603–04. The SEC seems to have the attitude that convergence will ultimately lead to total equivalence. *Id.* Thus, as of this writing, it does not seem to be actively pursuing equivalence with IFRS, and in any case, the SEC’s cooperation with the IASB, which is not an EU institution, falls outside the scope of this Note.

84. Atkins Speech, University of Gent, *supra* note 46, at 6.

85. *Id.* More bluntly stated: “It is not an important step [in the roadmap for ending reconciliation], in fact not a step at all, that IFRS be exactly the same as U.S. GAAP.” John W. White, Dir., Div. of Corp. Fin., Sec. & Exch. Comm’n, Remarks Before the Practising Law Institute Sixth Annual Institute on Securities Regulation in Europe (Jan. 15, 2007), available at <http://www.sec.gov/news/speech/2007/spch011507jww.htm> [hereinafter White Speech].

86. The CESR is separate from the EC, yet the EC can participate “actively” in its activities. Its responsibilities include “advis[ing] the European Commission on securities policy issues” and “develop[ing] effective operational network mechanisms to enhance day-to-day consistent supervision and enforcement of the Single Market for financial services.” Charter of the Committee of European Securities Regulators (July 2006), arts. 3, 4, available at <http://www.cesr.eu/index.php?page=cesrinsshort&mac=0&id=>. In other words, the CESR is somewhat similar to the American FASB since both are independent organizations that set accounting standards.

cooperation.”⁸⁷ The Work Plan imposes this structure by setting out “next steps” with timelines. These next steps pave the way for the SEC to accept IFRS financial reports and for the EC to accept financial reports compiled through U.S. GAAP standards. These steps range from sharing views on the future development of IFRS and U.S. GAAP, to consulting with each other on how the other’s standard applies to unprecedented questions or issues in which U.S. and EU standards conflict.⁸⁸ This last step is especially important to ensure consistent application of the standards, regardless of which agency is applying them.⁸⁹ Crucially, the Work Plan also sets out a schedule to facilitate dialog through semiannual meetings and ad hoc meetings as necessary.⁹⁰ As of this writing, the Plan’s success is currently being tested, since 2005 was the first year in which EU issuers registered in the United States would be able to file financial reports with the SEC using the IFRS system.⁹¹ The parties have stuck to their meeting schedule, even meeting on occasions not required by the Plan.⁹² Overall,

87. The Work Plan sets out four goals:

- Promote the development of high quality accounting standards;
- Promote the high quality and consistent application of IFRS around the world, and as a result move toward achieving this milestone under the roadmap; and
- Recognising that IFRS are principles-based standards, give full consideration to international counterparts’ positions regarding application and enforcement;
- Seriously endeavor to avoid conflicting regulatory decisions on the application of IFRS and US GAAP.

CESR-SEC Work Plan, art. I.A., Aug. 2, 2006, *available at* <http://www.focusifrs.com/content/download/1890/9377/version/1/file/WorkPlan.pdf>.

88. *Id.* arts. I.B.–C.

89. *Id.* Note that inconsistent application of accounting standards not only goes against the whole idea of allowing a company to use basically the same financial statement in both the United States and EU, but it risks eviscerating the substance of the accounting system used. Given the recent implementation of IFRS in the EU, differences in interpreting IFRS could be especially problematic. Tafara, for example, has voiced concern that IFRS may turn out to be less of a single international accounting standard and more of a “multiplicity of standards going by the same name.” Ethiopis Tafara, Dir., Office of Int’l Affairs, SEC, Remarks Before the Federation of European Accountants: International Financial Reporting Standards and the US Capital Market (Dec. 1, 2005), *available at* <http://www.sec.gov/news/speech/spch120105et.htm>. According to Tafara, the risks of divergent interpretations of IFRS “are not that IFRS are of insufficient quality to provide US investors with adequate information about an issuer. Rather, it is that financial statements prepared using IFRS cannot be compared to one another.” *Id.*

90. Charter of the Committee of European Securities Regulators, *supra* note 86, art. I.D.

91. Atkins Speech, University of Gent, *supra* note 46, at 5–6. Commissioner Atkins expected over three hundred filers to take advantage of the new option. *Id.* By January of 2007, the SEC and CESR had only undertaken “limited filing-specific contacts with foreign regulators about IFRS financial statements.” White Speech, *supra* note 85. This evaluation, however, reflects the state of contacts early in the review process: “We [the SEC] expect more of these contacts to arise naturally in the coming months as we finish up many more reviews. We look forward to those contacts, and we take very seriously our obligation to enter into them with an open mind.” *Id.*

92. In addition to the CESR-mandated meetings, the SEC held a Roundtable discussion in March

the SEC and EC's commitment to achieving mutual recognition "remains as strong as ever"⁹³ and both sides are likely to abolish reconciliation requirements by 2009.⁹⁴

C. *Evaluating Cooperation on Accounting Standards*

In their efforts at mutual recognition, the EC and SEC have embarked on a path of cooperation on the substance of regulations and, consequently, on the enforcement end of determining how to apply those standards. This is much higher-intensity, higher-commitment cooperation than the SEC and EC undertook to tackle deregistration. Not only did they commit themselves to regular meetings, but they are in the process of adopting rules recognizing each other's standards and—to the extent that one agency defers to the other's judgment on how to apply the other's accounting standard—they have set goals which require some, if not total, delegation and interdependence on matters of enforcement.

Though cooperation on accounting standards is still being tested, it seems to have worked well so far. Notably, this cooperation has proceeded without resorting to higher intensity means, like a uniform international accounting standard. In fact, the SEC and EC consciously chose mutual recognition as a better policy alternative than adopting a uniform standard. This, however, is not to say some more extreme method could not have been used to solve the problem (or will not be used in the future after the agencies have further tested the waters of cooperation).

V. CONCLUSION

This study shows that, while the world may be getting smaller, it is not necessarily becoming more uniform. Cooperation between the United States and EU on securities regulation has been focused on the specific problems at hand and results desired. In the case of the foreign issuer deregistration problem, for example, the SEC and EC worked together in a low-commitment, low-intensity manner limited to American policy development and adoption. Although the SEC and EC's cooperative

2007 on the ramifications of allowing financial reports to be filed using both IFRS and U.S. GAAP standards. This Roundtable featured all but one of the SEC Commissioners, and, notably, the EC's Commissioner McCreevy spoke at the event. Sec. & Exch. Comm'n, Transcript of International Financial Reporting Standards Roadmap Roundtable (Mar. 6, 2007), *available at* <http://www.sec.gov/spotlight/ifrsroadmap/ifrsroadmap-transcript.txt> [hereinafter IFRS Roundtable].

93. White Speech, *supra* note 85.

94. McCreevy Speech, U.S. Chamber, *supra* note 2, at 4.

efforts to do away with the reconciliation of accounting statements have involved much higher-intensity and higher-commitment work, the parties have set their sights on mutual recognition, rather than uniformity of regulations, and to the extent practicable, they have kept enforcement at a national level. Thus, there is no one perfect way for securities regulators to cooperate and more cooperation is certainly not always better cooperation.

To be certain, the cooperation between the SEC and EC described here can only increase the chances of more successful cooperation in the future. Throughout their efforts, the parties have acted cordially and candidly as neighbors, rather than as rivals trying to impose their way of doing things on the other party.⁹⁵ Officials from the SEC and EC have given numerous speeches on both sides of the Atlantic and have met in various meetings, roundtables, and teleconferences, always regarding the other party with an air of friendship and voicing criticisms in a constructive manner. The relevant actors seem familiar with each other and eager to share opinions. Of course, their interests are aligned on these issues through a common understanding of the problems facing transatlantic markets, but the trust and respect the parties have gained for each other can only help them work together through even more intractable issues in the future.

*Dania S. Becker**

95. Chairman Cox's comments on accounting standards highlight the collegial spirit between the SEC and EC:

The process is very much collaborative, and it recognizes that, by their very nature, neither IFRS nor U.S. GAAP is the exclusive purview of a particular regulator, but, rather, they are public goods for the common benefit of many. By consulting with each other, the SEC and the CESR staff can help ensure that high-quality global accounting standards are consistently interpreted and faithfully applied.

IFRS Roundtable, *supra* note 92. Commissioner McCreevy noted in a speech the next day that the progress of the past five years "is not a case of a European victory. It is the case of the markets leading and regulators sensibly following." McCreevy Speech, Building the Transatlantic Marketplace, *supra* note 27, at 2.

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