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**SECURITIES AND EXCHANGE COMMISSION**

**17 CFR Parts 200, 232, and 249**

**[Release No. 34-93701; IC-34431; File No. S7-03-21]**

**RIN 3235-AM84**

**Holding Foreign Companies Accountable Act Disclosure**

**AGENCY:** Securities and Exchange Commission.

**ACTION:** Final rule.

**SUMMARY:** We are adopting amendments to finalize interim final rules that revised Forms 20-F, 40-F, 10-K, and N-CSR to implement the disclosure and submission requirements of the Holding Foreign Companies Accountable Act (“HFCA Act”). The final amendments apply to registrants that the Securities and Exchange Commission (“Commission”) identifies as having filed an annual report with an audit report issued by a registered public accounting firm that is located in a foreign jurisdiction and that the Public Company Accounting Oversight Board (“PCAOB”) is unable to inspect or investigate completely because of a position taken by an authority in that jurisdiction. Consistent with the HFCA Act, the amendments require the submission of documentation to the Commission establishing that such a registrant is not owned or controlled by a governmental entity in that foreign jurisdiction and also require disclosure in a foreign issuer’s annual report regarding the audit arrangements of, and governmental influence on, such registrants.

**DATES:** The amendments are effective on January 10, 2022, except for the addition of §232.405(c)(1)(iii)(C), which is effective from January 10, 2022, until July 1, 2023.

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3430, in the Office of Rulemaking, Division of Corporation Finance; Theodore Venuti, Assistant Director, at (202) 551-5658, in the Office of Market Supervision, Division of Trading and Markets; or Blair Burnett, Senior Counsel, at (202) 551-6792, in the Investment Company Regulation Office, Division of Investment Management; U.S. Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549.

**SUPPLEMENTARY INFORMATION:** We are adopting amendments to the following rules and forms.

Commission Reference		CFR Citation (17 CFR)
Regulation S-T	Rule 405	§ 232.405
Securities Exchange Act of 1934 (Exchange Act) <sup>1</sup>	Form 20-F	§ 249.220f
	Form 40-F	§ 249.240f
	Form 10-K	§ 249.310
Exchange Act and Investment Company Act of 1940 (Investment Company Act) <sup>2</sup>	Form N-CSR	§§ 249.331 and 274.128

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<sup>1</sup> 15 U.S.C. 78a *et seq.*

<sup>2</sup> 15 U.S.C. 80a-1 *et seq.*

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## I. Introduction

On March 18, 2021,<sup>3</sup> the Commission adopted interim final amendments to Form 10-K, Form 20-F, Form 40-F, and Form N-CSR to implement the disclosure and submission requirements of Sections 2 and 3 of the HFCA Act,<sup>4</sup> which became law on December 18, 2020. Section 2 of the HFCA Act amended Section 104 of the Sarbanes-Oxley Act of 2002 (“Sarbanes-Oxley Act”)<sup>5</sup> by adding Section 104(i) to the Sarbanes-Oxley Act. Section 104(i)(2) of the Sarbanes-Oxley Act requires the Commission to identify each “covered issuer”<sup>6</sup> that has retained

<sup>3</sup> See *Holding Foreign Companies Accountable Act Disclosure*, Release No. 34-91364 (Mar. 18, 2021) [86 FR 17528 (Apr. 5, 2021)] (“Interim Final Release”).

<sup>4</sup> Pub. L. 116-222, 134 Stat. 1063 (Dec. 18, 2020).

<sup>5</sup> 15 U.S.C. 7214 (as amended by Pub. L. 116-222).

<sup>6</sup> See Section 104(i)(1)(A) of the Sarbanes-Oxley Act (defining a “covered issuer” as an issuer that is required to file reports under Section 13 (15 U.S.C. 78m) or Section 15(d) (15 U.S.C. 78o(d)) of the Exchange Act). In this release, we refer to issuers filing Exchange Act reports as “registrants.” We use the term “issuers” when referring to the HFCA Act, but refer to “registrants” when discussing the forms and form requirements.

a registered public accounting firm<sup>7</sup> to issue an audit report<sup>8</sup> where that registered public accounting firm has a branch or office<sup>9</sup> that:

- Is located in a foreign jurisdiction; and
- The PCAOB has determined that it is unable to inspect or investigate completely because of a position taken by an authority in the foreign jurisdiction.<sup>10</sup>

Once identified, Section 104(i)(2)(B) of the Sarbanes-Oxley Act requires these covered issuers, which we refer to as “Commission-Identified Issuers” in this release, to submit documentation to the Commission establishing that they are not owned or controlled by a governmental entity in that foreign jurisdiction.<sup>11</sup> Additionally, Section 3 of the HFCA Act lists

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<sup>7</sup> We use the terms “registered public accounting firm” and “auditor” interchangeably to mean public accounting firms that, among other things, prepare accountant’s reports on U.S. public companies and are required to register with the PCAOB. The term “accountant’s report” is defined in 17 CFR 210.1-02(a)(1) (Rule 1-02(a)(1) of Regulation S-X), with regard to financial statements, as a document in which an independent public or certified public accountant indicates the scope of the audit (or examination) that the accountant has made and sets forth that accountant’s opinion regarding the financial statements taken as a whole, or an assertion to the effect that an overall opinion cannot be expressed.

<sup>8</sup> The HFCA Act uses the term “audit report.” As noted above, *see supra* note 7, for the purposes of this release and the final amendments, the term “audit report” has the same meaning as “accountants’ report” in Rule 1-02(a)(1) of Regulation S-X.

<sup>9</sup> Where a branch or office of an international firm network is a separate legal entity from the U.S.-based or international firm network, and that branch or office signs the audit report in its own name, the Commission will look to the PCAOB determination for that branch or office and not apply that determination to the U.S.-based or other branches or offices of that firm network that are not based in the PCAOB-identified foreign jurisdiction.

<sup>10</sup> On September 22, 2021, the PCAOB adopted PCAOB Rule 6100, *Board Determinations Under the Holding Foreign Companies Accountable Act*, which was approved by the Commission on November 4, 2021. *See Public Company Accounting Oversight Board; Order Granting Approval of Proposed Rule Governing Board Determinations Under the Holding Foreign Companies Accountable Act*, Release No. 34-93527 (Nov. 4, 2021) [86 FR 62581 (Nov. 10, 2021)]. The PCAOB Rule 6100 establishes a framework for the PCAOB to make its determinations required by the HFCA Act. Specifically, PCAOB Rule 6100 establishes the manner of the PCAOB’s determinations; the factors the PCAOB will evaluate and the documents and information it will consider when assessing whether a determination is warranted; the form, public availability, effective date, and duration of such determinations; and the process by which the PCAOB will reaffirm, modify, or vacate any such determinations. In this release, we refer to a registered public accounting firm that the PCAOB has determined that it is unable to inspect or investigate completely because of a position taken by an authority in the foreign jurisdiction as a “PCAOB-Identified Firm.”

<sup>11</sup> In addition to this submission requirement, pursuant to Section 104(i)(3) of the Sarbanes-Oxley Act, as added by Section 2 of the HFCA Act, if an issuer is a Commission-Identified Issuer for three consecutive years, the Commission must prohibit the securities of the issuer from being traded on a national securities exchange or

additional disclosure requirements for Commission-Identified Issuers that are “foreign issuers”<sup>12</sup> (“Commission-Identified Foreign Issuers”).

We received a number of comment letters in response to the interim final amendments. While several commenters generally supported them,<sup>13</sup> some provided specific suggestions on how to improve them or otherwise implement the HFCA Act,<sup>14</sup> and others opposed<sup>15</sup> the interim final amendments. Generally, commenters supporting the interim final amendments stated that the amendments effectively provided for timely implementation of the HFCA Act<sup>16</sup> and also informed investors about the level of ownership and control the Chinese Government has in listed companies.<sup>17</sup> Additionally, commenters supporting the interim final amendments asserted that they agreed with the objective of the HFCA Act and were concerned about the lack of transparency into Chinese companies.<sup>18</sup>

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through any other method that is within the jurisdiction of the Commission to regulate, including through “over-the-counter” trading. 15 U.S.C. 7214(i)(3).

<sup>12</sup> See 17 CFR 240.3b-4 (“Exchange Act Rule 3b-4”). Under Exchange Act Rule 3b-4, the term “foreign issuer” means any issuer that is a foreign government, a national of any foreign country, or a corporation or other organization incorporated or organized under the laws of any foreign country.

<sup>13</sup> See letters from American Securities Association (May 5, 2021) (“ASA”), Council of Institutional Investors (May 5, 2021) (“CII”), U.S. Chamber of Commerce (May 21, 2021) (“Chamber”), United States Senator Dan Sullivan *et al.* (Aug. 9, 2021) (“Sen. Sullivan *et al.*”), and United States Senator John Kennedy (Apr. 28, 2021) (“Sen. Kennedy”).

<sup>14</sup> See letters from ICI Global (May 5, 2021) (“ICI”), Jessica Kelly (Apr. 30, 2021) (“Kelly”), Professor Curtis J. Milhaupt and Professor Lauren Yu-Hsin Lin (Apr. 5, 2021) (“Profs. Milhaupt and Lin”), New York Stock Exchange LLC (May 12, 2021) (“NYSE”), and Professor Emmanuel T. De George *et al.* (May 4, 2021) (“U.S. Acctg. Academics”).

<sup>15</sup> See letters from Blank Rome LLP (May 5, 2021) (“Blank Rome”); China Petroleum & Chemical Corporation (Apr. 30, 2021) (“China Petroleum”); China Southern Airlines Company Limited (Apr. 30, 2021) (“China Southern”); Professor Jie *et al.* (May 3, 2021) (“Chinese Legal Academics”); Shanshan Xu (May 2, 2021) (“Xu”); and Yum China Holdings, Inc. (May 4, 2021) (“Yum”).

<sup>16</sup> See, e.g., letter from ICI.

<sup>17</sup> See, e.g., letter from ASA.

<sup>18</sup> See, e.g., letter from Chamber.

On the other hand, commenters opposing the amendments stated that the amendments were repetitive of disclosure that is already provided and would result in unnecessary compliance costs,<sup>19</sup> were unfair to Chinese registrants,<sup>20</sup> may bring adverse effects to the interests of global investors in Commission-Identified Issuers,<sup>21</sup> and did not account for regulations in other jurisdictions.<sup>22</sup> Some of these commenters also argued that any conflicts of relevant laws in different jurisdictions that inhibit PCAOB inspection should be resolved through the cooperation of regulators from the different jurisdictions.<sup>23</sup> Many of these comments reflect general opposition to the design and operation of the HFCA Act itself. Where commenters addressed aspects of the statute that Congress left to the Commission to implement, we have responded to those comments below, in our discussion of the final amendments.

## **II. Discussion of Amendments**

### **A. Documentation Submission Requirements**

#### **1. Interim Final Amendments**

As discussed above, Section 2 of the HFCA Act amended Section 104(i)(2) of the Sarbanes-Oxley Act to require any Commission-Identified Issuer to submit to the Commission documentation establishing that the issuer is not owned or controlled by a governmental entity in the relevant foreign jurisdiction.<sup>24</sup> The Commission amended Form 10-K, Form 20-F, Form 40-

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<sup>19</sup> See letter from China Petroleum.

<sup>20</sup> See letters from Chinese Legal Academics and China Petroleum.

<sup>21</sup> See letters from Blank Rome, Chinese Legal Academics, China Southern, and Yum.

<sup>22</sup> See letters from China Southern and Xu.

<sup>23</sup> See letters from Blank Rome, Chinese Legal Academics, China Southern, China Petroleum, and Xu.

<sup>24</sup> See Section 104(i)(2)(A) of the Sarbanes-Oxley Act. The interim final amendments met the Section 104(i)(4) of the Sarbanes-Oxley Act mandate that the Commission adopt rules establishing the manner and form in which such submissions will be made no later than 90 days after enactment.

F, and Form N-CSR to implement this provision. The submission requirement applies to all Commission-Identified Issuers. The interim final amendments required this documentation to be submitted electronically to the Commission on a supplemental basis<sup>25</sup> through the Electronic Data Gathering, Analysis, and Retrieval (“EDGAR”) system on or before the due date of the relevant annual report form.

Although the interim final amendments prescribed the timing and means by which such submissions were made, neither they nor the HFCA Act specified the particular types of documentation that could or should be submitted for this purpose. Moreover, in the Interim Final Release, the Commission recognized that available documentation could vary depending upon the organizational structure and other factors specific to the registrant. Thus, registrants had flexibility under the interim final amendments to determine how best to satisfy this requirement.

## **2. Comments**

One commenter recommended that registrants make the submission of documentation establishing that the issuer is not owned or controlled by a governmental entity in the foreign jurisdiction of the PCAOB-Identified Firm in the form of a certification, but did not support requiring the submission to be filed in a Form 8-K because it should not be classified as a “material event” and did not support requiring disclosure that a registrant is a Commission Identified issuer under Form 8-K.<sup>26</sup> This commenter suggested that making the submission publicly available or filed as an exhibit would exceed the actions authorized by the HFCA Act

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<sup>25</sup> For purposes of the interim final amendments, use of the term “supplemental” did not have the meaning of “supplemental information” in 17 CFR 240.12b-4. This is true for the final amendments we are adopting in this release as well.

<sup>26</sup> See letter from Yum.

and indicated that registrants may wish to seek confidential treatment for some or all of the submission. The commenter also suggested that we establish a universal due date for the submission requirement that is later than the due date for the annual report to provide registrants additional time to prepare the submission and reduce the costs of compliance, and that we should not make the determinations of Commission-Identified Issuers more often than annually.

Additionally, the commenter recommended that a registrant retain flexibility over the type of documentation a Commission-Identified Issuer must submit to establish that it is not owned or controlled by a governmental entity in the foreign jurisdiction based on its facts and circumstances, but indicated that publication of non-exclusive methods to satisfy the requirement would be valuable. This commenter suggested potential non-exclusive methods to show there is no ownership or control, such as there has been no Schedule 13D or 13G filing by a government related entity in the foreign jurisdiction, there are no material contracts with a foreign governmental party, or there is no foreign government representative on the board.

Another commenter recommended additional guidance on the meaning of “owned or controlled.”<sup>27</sup> The commenter suggested that the amendments use the term “significant influence” under U.S. Generally Accepted Accounting Principles (“U.S. GAAP”) and incorporate specific examples including: (1) where a government entity or affiliate has 20 percent or greater ownership or voting interest; (2) existence and effect of potential voting rights that are currently exercisable or convertible; (3) when an entity is represented on the board of directors or equivalent governing body of the investee entity; and (4) an entity’s participation in policy-making processes, including participation in decisions about dividends or other distributions.

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<sup>27</sup> See letter from U.S. Acctg. Academics.

### 3. Final Amendments

We are finalizing the interim final amendments with respect to the submission requirements without modification. The amendments require any Commission-Identified Issuer to submit to the Commission through EDGAR,<sup>28</sup> on or before the due date of the relevant annual report form, documentation establishing that the issuer is not owned or controlled by a governmental entity in the foreign jurisdiction of the PCAOB-Identified Firm. This submission will be made publicly available on EDGAR, which we believe is consistent with the HFCA Act given its focus on transparency.<sup>29</sup>

Additionally, the final amendments continue to permit Commission-Identified Issuers to determine the appropriate documentation to submit in response to the requirement, based on their organizational structure and other registrant-specific factors. We decline to provide an exclusive or non-exclusive list of what documentation may demonstrate that the registrant is not owned or controlled by the relevant governmental entity. We believe that such a list may be too limiting or become the *de facto* means of satisfying the requirement. We believe that Commission-Identified Issuers should instead make a determination of what documentation meets the requirement for their particular company. We also believe that not prescribing the specific documentation Commission-Identified Issuers must submit will limit compliance costs and could result in more relevant information being provided to investors.

Moreover, although the terms are not defined in the statute, we believe that the meaning of the terms “owned or controlled,” “owned,” and “controlling financial interest” in the HFCA

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<sup>28</sup> The final amendments do not specify the manner in which a registrant must submit the required documentation on EDGAR. A registrant could submit the documentation with its annual report; on Forms 8-K or 6-K, as applicable; or using another appropriate method.

<sup>29</sup> *See* letter from Sen. Kennedy (stating that the purpose of the legislation “is to make relevant information about publicly traded firms explicit and easily accessible to investors”).

Act reference a person’s or governmental entity’s ability to “control” the registrant as that term is used in the Exchange Act and the Exchange Act rules.

One commenter suggested that the amendments use the term “significant influence” under U.S. GAAP and incorporate a specified list of examples. We note, however, that the HFCA Act refers to the Exchange Act and the Commission’s Exchange Act rules. Therefore, we believe the terms “owned or controlled,” “owned,” and “controlling financial interest” used in the HFCA Act are reasonably read to have the same meaning as the term “control” as used in the Exchange Act and the Exchange Act rules. Moreover, registrants should generally understand the concept of “control” and so incorporating the same meaning will result in consistent application of the concept across different regulatory contexts.

## **B. Disclosure Requirements**

### **1. Interim Final Amendments**

Section 3 of the HFCA Act requires a Commission-Identified Foreign Issuer to provide the following additional disclosures in its annual report for the year that the Commission so identifies the issuer:<sup>30</sup>

- That, during the period covered by the form, the PCAOB-Identified Firm that has prepared an audit report for the issuer;<sup>31</sup>

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<sup>30</sup> The HFCA Act requires these disclosures in the issuer’s Form 10-K, Form 20-F, or a form that is the equivalent of, or substantially similar to, these forms. The disclosures required by Section 3 of the HFCA Act are also required in transition reports filed on Forms 10-K and in transition reports on Form 20-F that include audited financial statements. The disclosures should address the transition period as if it were a fiscal year.

<sup>31</sup> The registered public accounting firm referenced in the statute means a PCAOB-Identified Firm. *See supra* notes 7 through 10. The interim final amendments included slightly different terms than those in the statutory language to clarify this and other points. Specifically, the interim final amendments required a Commission-Identified Foreign Issuer to disclose that, for the immediately preceding annual financial statement period, a registered public accounting firm that the PCAOB was unable to inspect or investigate completely, because of a position taken by an authority in the foreign jurisdiction, issued an audit report for the registrant. For the same reasons, the final amendments include the same terms used in the interim final amendments for clarification as well.

- The percentage of the shares of the issuer owned by governmental entities in the foreign jurisdiction in which the issuer is incorporated or otherwise organized;
- Whether governmental entities in the applicable foreign jurisdiction with respect to that registered public accounting firm have a controlling financial interest with respect to the issuer;
- The name of each official of the Chinese Communist Party (“CCP”) who is a member of the board of directors of the issuer or the operating entity with respect to the issuer; and
- Whether the articles of incorporation of the issuer (or equivalent organizing document) contains any charter of the CCP, including the text of any such charter.

Although Section 3 of the HFCA Act does not mandate specific rule or form changes, the Commission stated its belief in the Interim Final Release that amending Commission forms to include the new disclosure requirements will help registrants comply with the HFCA Act. The Commission therefore amended Form 10-K, Form 20-F, Form 40-F,<sup>32</sup> and Form N-CSR<sup>33</sup> to reflect the disclosure requirements in Section 3 of the HFCA Act.

The interim final amendments required a registrant to provide the disclosure for each year in which the registrant is a Commission-Identified Foreign Issuer. Because the period covered

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<sup>32</sup> As we noted in the Interim Final Release, in reviewing the Commission’s forms, we determined that Form 40-F is an equivalent or substantially similar form filed by foreign issuers. The Form 40-F is a form that may be used by Canadian issuers that seek to offer their securities in the United States and is used by those issuers for annual reports filed under Section 13(a) or Section 15(d) of the Exchange Act. As such, even though the form is not expressly named in the HFCA Act, its use by issuers for annual reports filed under Section 13(a) and Section 15(d) establishes the form as equivalent or substantially similar to the Form 10-K and Form 20-F.

<sup>33</sup> Form N-CSR is an annual reporting form used by registered investment companies that are affected by the HFCA Act to file their audited financial statements with the Commission. Although Form N-CSR is not specifically identified in the HFCA Act, as we indicated in the Interim Final Release, its use by these registered investment companies for annual reports filed under Section 13(a) and Section 15(d) establishes the form as equivalent or substantially similar to the Form 10-K and Form 20-F.

by the forms looks back at the prior year, a Commission-Identified Foreign Issuer that was identified in the prior year would have been required to provide the HFCA Act Section 3 disclosure in its annual report for the year in which it was identified, even if the registrant's subsequent filing includes an audit report issued by a registered public accounting firm that is a not a PCAOB Identified Firm ("non-PCAOB Identified Firm").

In addition, the interim final amendments added an instruction in each of Form 20-F and Form 40-F to specify that the disclosure applies to annual reports, and not to registration statements.<sup>34</sup>

## 2. Comments

Commenters in one letter stated that registrants typically are not providing the detailed disclosures required by the HFCA Act and that current risk factor disclosure tends to be insufficient for investors to understand the consequences of non-inspection.<sup>35</sup> Other commenters in a separate letter recommended that the disclosure requirement relating to identification of officials of the CCP that are members of the board of directors is vague and may be unhelpful because the concept of "official of the CCP" is susceptible to variation.<sup>36</sup> The commenter stated that virtually all executives of Chinese state-owned enterprises are members of the CCP as are many executives of private firms. This commenter further stated that very little information about the degree of control exercised by the Chinese Government and CCP over a registrant can be gleaned solely from disclosure of a reference to the CCP charter in the company's articles of

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<sup>34</sup> While Form 20-F and Form 40-F may be used as an initial registration form, the Commission noted its belief in the Interim Final Release that, in the context of Section 3 of the HFCA Act, which linked the Form 20-F requirement to the Form 10-K requirement, the disclosure was intended to be required when the form is used as an annual report.

<sup>35</sup> See letter from U.S. Acctg. Academics.

<sup>36</sup> See letter from Profs. Milhaupt and Lin.

incorporation.

The commenter recommended requiring disclosure of each board member's current and past positions and ranks within the Chinese Government or CCP and whether the board member serves on the registrant's internal Communist Party Committee (suggesting such disclosure would provide material information about an individual's links to the Chinese party-state and, by extension, the degree of influence the party-state exerts over the company). Additionally, the commenter recommended disclosure of all provisions in a registrant's articles of incorporation that reference the CCP or the company's internal Communist Party Committee.

This commenter stated that since many companies with Chinese operations are listed in the United States using variable interest entity ("VIE") structures incorporated in jurisdictions outside of China, the disclosure requirements could be read as not requiring disclosure of Chinese Government ownership of shares of the registrant. The commenter recommended that the amendments clarify that "Commission-Identified Foreign Issuers are required to disclose the percentage of shares of the registrant owned by governmental entities in the foreign jurisdiction in which the registrant is incorporated or otherwise organized, or in which the registrant's operating entity is incorporated."

Another commenter recommended that the Commission consider whether risks are heightened for registrants using a VIE structure, given that the structure could block meaningful disclosure of financial and political information.<sup>37</sup> A different commenter also noted concerns with VIE and dual-class structures, which are complex and involve risks that the commenter believes are not fully understood by many market participants.<sup>38</sup> This commenter recommended

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<sup>37</sup> See letter from Kelly.

<sup>38</sup> See letter from CII.

additional disclosure guidance for VIE and dual-class stock structures for investors to more fully understand the ownership or control of those registrants subject to the HFCA Act.

Moreover, one commenter suggested that we consider distinguishing registrants that list exclusively on a U.S. exchange from those that have a secondary listing overseas, noting the Commission’s assessment in the Interim Final Release that 79 percent of registrants covered by the HFCA Act disclose listing only on a U.S. national exchange.<sup>39</sup> Another commenter suggested vigilance relating to firms that switch between U.S. and foreign jurisdictions to reset the clock or switch to auditors operating only nominally in the United States.<sup>40</sup>

### **3. Final Amendments**

We are finalizing the disclosure requirements for Commission-Identified Foreign Issuers with a minor modification to the interim final amendments. As with the interim final amendments, we are adopting amendments to Form 10-K to revise Part II, Item 9C, Form 20-F to revise Part II, Item 16I, Form 40-F to revise paragraph B.18, and Form N-CSR to revise paragraph (j) of Item 4. The amended language in these forms is the same as the language in the interim final amendments, with the exception of the modification pertaining to VIE structures described below, and requires a Commission-Identified Foreign Issuer to provide the disclosures discussed above that are required by the HFCA Act.<sup>41</sup>

We do not believe it is necessary to explain further what is meant by “official of the CCP” or require additional disclosures relating to this matter at this time. We believe the term is clear from the HFCA Act and our amendments. Moreover, we are not adopting additional disclosure requirements suggested by some commenters, as they would exceed the HFCA Act’s

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<sup>39</sup> See letter from Kelly (citing Interim Final Release, *supra* note 3, at 17538, n. 54).

<sup>40</sup> See letter from U.S. Acctg. Academics.

<sup>41</sup> See *supra* Section II.B.1.

requirements and are outside the scope of this rulemaking.

We note commenters' concerns that the interim final amendments could be interpreted to mean that a Commission-Identified Foreign Issuer listed in the United States using VIE or similar corporate structures that is incorporated or otherwise organized in one jurisdiction, but that has a consolidated operating company incorporated or otherwise organized in another jurisdiction, may not be required to disclose government ownership of shares of the operating company.<sup>42</sup> That was not the intent of the interim final amendments, and we do not believe this is consistent with the intent of the HFCA Act. Therefore, we believe that a registrant should provide the required disclosure associated with a consolidated operating company through a VIE structure or other similar structures. Also, we do not believe that a registrant should be able to avoid the HFCA Act's requirements by using a VIE structure or other similar structures.

Therefore, the final amendments modify the interim final amendments to make clear that the registrant must, in addition to providing the required disclosures for the Commission-Identified Foreign Issuer, look through a VIE or any structure that results in additional foreign entities being consolidated in the financial statements of the registrant and provide the required disclosures about any consolidated operating company or companies in the relevant jurisdiction. Thus, the amended forms state that any Commission-Identified Foreign Issuer that uses a VIE or any structure that results in additional foreign entities being consolidated in the financial statements of the registrant must provide the required disclosures for itself and its consolidated foreign operating entities.

### **C. Inline XBRL Tagging**

In the Interim Final Release, we sought comment on whether to introduce structured data

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<sup>42</sup> See letters from CII, Kelly, and Profs. Milhaupt and Lin.

tagging requirements pertaining to the auditor name and jurisdiction on the audit report signed by the registered public accounting firm in the registrant’s Form 10-K, Form 20-F, and Form 40-F. We suggested that such tagging would provide machine-readable data directly from the registrant identifying the audit firm retained by it, and may therefore facilitate the Commission’s determination of the registrants it should designate as Commission-Identified Issuers. Two commenters recommended an eXtensible Business Reporting Language (“XBRL”) structured tagging requirement.<sup>43</sup> One of these commenters recommended tagging the auditor name, branch office, and PCAOB jurisdiction as listed on the Form AP, and the other commenter suggested tagging the auditor’s name and jurisdiction as set forth on the audit report.<sup>44</sup>

Consistent with these commenters’ suggestions, the final amendments include a new tagging requirement to facilitate the Commission’s accurate and efficient identification of Commission-Identified Issuers. To implement this requirement, in December 2021, the Document Entity and Information (“DEI”) taxonomy will be updated to include three additional data elements, applicable to annual report filings on Forms 10-K, 20-F, and 40-F that are submitted with XBRL presentations.<sup>45</sup> Those three data elements will identify the auditor (or auditors) who have provided opinions related to the financial statements presented in the registrant’s annual report, the location where the auditor’s report has been issued, and the PCAOB ID Number(s) of the audit firm(s) or branch(es) providing the opinion(s).

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<sup>43</sup> See letters from U.S. Acctg. Academics and CII.

<sup>44</sup> See letter from U.S. Acctg. Academics.

<sup>45</sup> We expect that the revised DEI Taxonomy will be published as “dei-2021q4.” A draft of the taxonomies was published for comment on September 1, 2021 at <https://xbrl.sec.gov/dei/2021q4/>. See *DRAFT 20201Q4 and Draft 2022 SEC Taxonomies*, available at <https://www.sec.gov/structureddata/announcement/osd-announcement-081621-draft-cef-and-vip-taxonomies-update>. See Also *Release Notes for CEF and DEI Taxonomies 2021Q4 DRAFT*, U.S. SEC. EXCH. & COMM’N (Sept. 1, 2021), available at <https://xbrl.sec.gov/doc/releasenotes-2021q4-draft.pdf>. We are not making similar updates to the DEI taxonomy for Form N-CSR because the Commission currently collects on Form N-CEN (referenced in 17 CFR 249.330) information regarding a fund’s auditor in a structured data format.

When the updated DEI taxonomy is published, deployed to EDGAR, and announced as part of the newly-adopted EDGAR Filer Manual for the relevant release in December 2021, all registrants will be required to use the updated taxonomy, or a subsequently adopted version of the taxonomy, for any annual report filed for a period ended after December 15, 2021.

We are adding a new paragraph to Rule 405 of Regulation S-T to clarify that registrants must use the new data elements. The paragraph will remain part of Regulation S-T until the 2021 DEI taxonomy has been removed from EDGAR in 2023. Because we are not adopting a change to the underlying forms, for registrants that are filing their financial statements using Inline XBRL, the final amendments leave placement of the underlying tags within the annual report up to the registrant.<sup>46</sup>

#### **D. Timing Issues**

The HFCA Act was enacted on December 18, 2020 and provides for identification of the issuers required to file reports under Section 13 or 15(d) of the Exchange Act during a year that begins “after the date of enactment” of the HFCA Act. Given this statutory language, and in response to some commenters,<sup>47</sup> we reiterate that a registrant will not be subject to a non-inspection year determination for any fiscal year ending on or prior to December 18, 2020. Accordingly, the Commission will identify registrants pursuant to the HFCA Act based on the PCAOB’s determination and on registrants’ annual reports for fiscal years beginning after December 18, 2020. The earliest that the Commission could identify a Commission-Identified Issuer would be after registrants file their annual reports for 2021 and identify the accounting

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<sup>46</sup> The new DEI tagged data elements, particularly the PCAOB ID Number, are not new disclosure requirement themselves (*e.g.*, not changing the current form and content of the independent auditor’s report), but are necessary for EDGAR and the staff to process the forms, akin to an EDGAR header data element. The data elements will to assist the Commission and its staff in performing the required identification activity required by the Act.

<sup>47</sup> *See* letters from ASA, Chamber, and NYSE.

firm that audited their financial statements.

A registrant will be required to comply with the submission and disclosure requirements in the annual report for each year in which it was so identified. This means that if a registrant is identified as being a Commission-Identified Issuer based on its annual report filing made in 2022 for the fiscal year ended December 31, 2021, the registrant will be required to comply with the submission and, if applicable, the disclosure requirements in its annual report filing covering the fiscal year ended December 31, 2022, that the registrant is required to file in 2023.

#### **E. Determination of Commission-Identified Issuer**

In the Interim Final Release, the Commission stated that it will provide appropriate notice once it has established the process by which it will begin to identify registrants pursuant to the HFCA Act. In this regard, the Commission acknowledged that a registrant will not be required to comply with the submission or disclosure requirements until the Commission identifies a registrant as having a non-inspection year. The Commission also indicated that it was considering making the determination of Commission-Identified Issuers on an annual basis based on the audit report contained in a registrant's annual report filed with the Commission for the most recently completed fiscal year preceding the date of the Commission determination. Additionally, the Commission stated that a registered public accounting firm is "retained" by a registrant, as that term is used in Section 104(i) of the Sarbanes-Oxley Act, when the registered public accounting firm signs the accountant's report on the registrant's consolidated financial statements that is included in a registrant's Exchange Act report. The Commission requested comment on whether it should publish a list of Commission-Identified Issuers on its website or whether Commission-Identified Issuers should be identified on EDGAR. Finally, the Commission asked how it should address any potential errors in identification relating to a

registrant's status if the list is made public and whether it should issue guidance or prescribe rules relating to disclosure or procedures for identification of errors relating to a registrant's status.

A few commenters suggested that the Commission should make the Commission-Identified Issuer determination based on the registrant's fiscal year end.<sup>48</sup> One commenter stated that the Commission should make determinations and provide notice to registrants as early as possible after a registrant's filing of its annual report.<sup>49</sup> Some commenters recommended publishing the list of Commission-Identified Issuers on the Commission's website,<sup>50</sup> while one commenter recommended providing the information on EDGAR for efficient and rapid identification.<sup>51</sup>

One commenter suggested that providing a list or identifying Commission-Identified Issuers on EDGAR is unnecessary and doing so would go beyond the statutory mandate.<sup>52</sup> Some commenters indicated that the Commission should notify directly any registrants that it has determined to be Commission-Identified Issuers prior to publishing the list, in light of the potential market impact on these issuers and to ensure accuracy of such a list.<sup>53</sup> Yet another commenter recommended that the Commission provide guidance rather than prescribe rules relating to disclosure or procedures to correct errors relating to the Commission's inclusion of a registrant on its Commission-Identified Issuer list to provide flexibility to the Commission and

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<sup>48</sup> See letters from Chamber (recommending 30 or 45 days after the filing deadline for the annual report), U.S. Acctg. Academics, and Yum.

<sup>49</sup> See letter from Yum.

<sup>50</sup> See letters from ASA, Chamber, and U.S. Acctg. Academics.

<sup>51</sup> See letter from CII.

<sup>52</sup> See letter from Yum.

<sup>53</sup> See letters from Chamber and Yum.

registrants.<sup>54</sup>

One commenter noted potential discrepancies between the three primary sources of public data that could be used to determine Commission-Identified Issuers: (1) the PCAOB's published list of audit reports in jurisdictions where authorities deny access, (2) the PCAOB's Form AP database, and (3) registrants' annual reports filed on EDGAR.<sup>55</sup> According to the commenter, these potential discrepancies raise a concern regarding the information on which the Commission would base its determination. The commenter also argued that, in situations with multiple audit reports in an annual report filing, the "retained" auditor should be "the auditor who signs off on the current (or more recent) fiscal-year financial statements."

Based on our further consideration and the input of commenters, we have determined to institute the following procedures for preparing and publishing the Commission-Identified Issuer list. We agree with the commenter who suggested that registrants should be identified as early as possible after the filing of an annual report and on a rolling basis.<sup>56</sup> Accordingly, promptly after the filing of an annual report, the Commission will evaluate, using Inline XBRL tagging or other structured data, whether the annual report contains an audit report signed by a PCAOB-Identified Firm.<sup>57</sup>

We continue to believe that a registered public accounting firm is "retained" by a registrant, as that term is used in Section 104(i) of the Sarbanes-Oxley Act, when the registered

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<sup>54</sup> See letter from Yum.

<sup>55</sup> See letter from U.S. Acctg. Academics.

<sup>56</sup> See *supra* note 49.

<sup>57</sup> In response to the commenter that raised concerns regarding the potential discrepancies between primary sources of data from which the Commission may generate its list, we note that we intend to base a determination on whether a registrant is a Commission Identified Issuer based on the audit report included in their annual report filing. We do not believe that the determination should be made based on Form AP filings because these are not filings made by the registrant.

public accounting firm signs the accountant’s report on the registrant’s consolidated financial statements that is included in a registrant’s Exchange Act report. However, we are taking a different approach than the one suggested by a commenter regarding instances where an annual report may contain multiple audit reports. In situations where an annual report for an issuer other than a registered investment company registrant organized as a series company contains multiple accountant’s reports or involves more than one registered public accounting firm, only the registered public accounting firm or firms that serve as “principal accountant” within the meaning of 17 CFR 210.2-05 (Rule 2-05 of Regulation S-X) and AS 1205: *Part of the Audit Performed by Other Independent Auditors* will, upon signing the accountant’s report on the registrant’s consolidated financial statements, be deemed “retained” for purposes of Section 104(i) of the Sarbanes-Oxley Act and the Commission’s determination of whether the registrant should be a Commission Identified Issuer. For a registered investment company registrant organized as a series company, each series will be deemed to “retain” the public accounting firm that signs the audit report for the series.

Once a registrant has been identified as described above,<sup>58</sup> the Commission<sup>59</sup> will “provisionally identify” such issuer as a Commission-Identified Issuer on the Commission’s website at [www.sec.gov/HFCAA](http://www.sec.gov/HFCAA). The Commission website will clearly delineate between provisional identifications and “conclusive identifications,” and registrants will not be a Commission-Identified Issuer until a conclusive determination has been made. For a period of

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<sup>58</sup> See *supra* Section II.D.

<sup>59</sup> As discussed below, *see infra* Section II.G, the Commission is adopting 17 CFR 200.30-1(m) (new Rule 30-1(m)) that delegates Commission authority to the Director of the Division of Corporation Finance to identify a registrant as a Commission-Identified Issuer.

15 business days<sup>60</sup> after the provisional identification, a registrant may contact the Commission by email<sup>61</sup> if it believes it has been incorrectly identified and may provide evidence supporting such claims. The Commission will respond to the registrant by email with respect to its analysis of such evidence and its determination. If the Commission agrees with the registrant's analysis, the Commission will notify the registrant and will remove the registrant from the provisional identification list. On the other hand, if the Commission does not agree that the registrant has been incorrectly identified, the determination that the registrant is a Commission-Identified Issuer will be conclusive. If the registrant does not contact the Commission to dispute the provisional identification, the determination that the registrant is a Commission-Identified Issuer will be conclusive 15 business days after the provisional identification.<sup>62</sup>

We did not accept the suggestion of one commenter that the staff contact each individual registrant that has been identified for inclusion in the list because we believe website posting will provide sufficient notice and we are concerned that such procedures could further delay issuer identification, which would be to the detriment of investors. Additionally, under the PCAOB Rule 6100, the PCAOB will notify each PCAOB-Identified Firm of its determination and will also publish the list on its website. As such, we do not believe provisional identification of issuers on the Commission website will have a significant additional market impact. Finally, we considered but determined not to publish the list of Commission-Identified Issuers on EDGAR. The EDGAR system is designed to retain filings by and about individual registrants, rather than present collated information. Consequently, the EDGAR system will not provide a mechanism

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<sup>60</sup> The term "business day" means any day, other than Saturday, Sunday, or a Federal holiday.

<sup>61</sup> The email address will be provided on the [www.sec.gov/HFCAA](http://www.sec.gov/HFCAA) website when or before the provisional Commission-Identified Issuer list is first populated.

<sup>62</sup> In no event would the conclusive determination be made before expiration of the 15-business-day period.

to publish a list on EDGAR that includes a number of registrants grouped together.

In addition to identifying Commission-Identified Issuers, the list published on the Commission website will indicate the number of consecutive years a Commission-Identified Issuer has been published on the list and whether it has been subject to any prior trading prohibitions under the HFCA Act. We believe it is appropriate to include this information on the list because of the significance of the trading prohibition requirements set forth in Section 104(i)(3) of the Sarbanes-Oxley Act, as discussed in greater detail below.<sup>63</sup>

## **F. Process for Trading Prohibition**

### **1. HFCA Act Trading Prohibitions**

Section 104(i)(3) of the Sarbanes-Oxley Act requires the Commission to prohibit the trading on a national securities exchange or through any other method which is within the jurisdiction of the Commission to regulate, including through over-the-counter trading, of the securities of certain Commission-Identified Issuers (“trading prohibition”). Section 104(i)(3)(A) of the Sarbanes-Oxley Act requires the Commission to impose a trading prohibition on a registrant that is determined to be a Commission-Identified Issuer for three consecutive years (“initial trading prohibition”). Section 104(i)(3)(B) of the Sarbanes-Oxley Act provides that the Commission shall end an initial trading prohibition if the issuer certifies to the Commission that it “has retained a registered public accounting firm that the [PCAOB] has inspected” to the satisfaction of the Commission.<sup>64</sup> Furthermore, if the Commission ends a trading prohibition under Section 104(i)(3)(B) of the Sarbanes-Oxley Act and, thereafter, the registrant is again determined to be a Commission-Identified Issuer, Section 104(i)(3)(C) of the Sarbanes-Oxley

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<sup>63</sup> See *infra* Section II.F.

<sup>64</sup> For purposes of terminating an initial trading prohibition or subsequent trading prohibition, the Commission will terminate the prohibition if the retained firm is a non-PCAOB-Identified Firm.

Act requires the Commission to impose on such issuer a trading prohibition for a minimum of five years (“subsequent trading prohibition”). Section 104(i)(3)(D) of the Sarbanes-Oxley Act provides that the Commission shall end a subsequent trading prohibition if, after the end of the five-year period, the issuer certifies to the Commission that it “will retain” a non-PCAOB-Identified Firm.<sup>65</sup>

In the Interim Final Release, the Commission specifically requested comment on any considerations it should take into account while determining how to best implement the trading prohibition requirements set forth in Section 104(i)(3) of the Sarbanes-Oxley Act.<sup>66</sup> A few commenters supported the prompt implementation of the trading prohibition.<sup>67</sup> One of these commenters suggested that any deferral of the commencement beyond 2024 would be inconsistent with the HFCA Act.<sup>68</sup>

Other commenters noted the importance of clear rules relating to the trading prohibition.<sup>69</sup> One of these commenters highlighted the importance of the Commission establishing a “transparent and well communicated” process with clear information and adequate notice of delisting to minimize disruption to investors in such entities.<sup>70</sup> This commenter indicated that a “transparent process that provides clear information and adequate notice” is necessary to provide market participants with the information they need to make investment decisions in a timely manner.

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<sup>65</sup> The five-year period begins on the date on which the Commission imposes a subsequent trading prohibition. *See* Section 104(i)(3)(D) of the Sarbanes-Oxley Act.

<sup>66</sup> *See* Interim Final Release *supra* note 3, at 17533.

<sup>67</sup> *See* letters from CII and Sen. Sullivan *et al.*

<sup>68</sup> *See* letter from CII.

<sup>69</sup> *See* letters from ICI and NYSE.

<sup>70</sup> *See* letter from ICI.

Another commenter recommended that the precise date on which any trading prohibition applies to an issuer's securities be made public by the Commission as soon as possible and that we allow no flexibility or ambiguity regarding the date on which the trading prohibition applies.<sup>71</sup> This commenter further recommended clarifying whether a trading prohibition would include derivatives, such as options and swaps based on the Commission-Identified Issuer's securities, and that the Commission should clearly establish the impact of a trading prohibition on any other securities market activities, such as clearance and settlement and options exercise and assignment. Another commenter stated that the Commission should take steps to prohibit the trading of Commission-Identified Issuer's securities on margin to avoid creating unnecessary risks that will disrupt markets and needlessly harm small investors and prohibit the inclusion of Chinese companies in passive index funds.<sup>72</sup> On the other hand, some commenters generally opposed the trading prohibition required by the HFCA Act, arguing that the trading prohibition would damage U.S. capital markets and harm U.S. investors.<sup>73</sup>

We agree with those commenters<sup>74</sup> who stated that the prompt implementation of the trading prohibition requirements of Section 104(i)(3) of the Sarbanes-Oxley Act is consistent

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<sup>71</sup> See letter from NYSE. This commenter recommended clarifying whether a trading prohibition would commence: (i) on January 1 of the third year following the Commission's determination that a registrant is a Commission-Identified Issuer; or (ii) three years after the date on which the Commission makes its determination that a registrant is a Commission-Identified Issuer. See also *infra* note 82 and accompanying text.

<sup>72</sup> See letter from ASA.

<sup>73</sup> See letters from Blank Rome, China Southern, Chinese Legal Academics, Kelly, and Yum.

<sup>74</sup> See *supra* notes 67 to 68. As noted above, the earliest that Commission could identify Commission-Identified Issuers would be after companies file their annual reports for 2021 and identify the accounting firm that audited their financial statements that, for calendar year issuers, would be spring of 2022. As a result, the earliest any trading prohibitions required by Section 104(i)(3) of the Sarbanes-Oxley Act would apply would be in 2024, once any issuer has been a Commission-Identified Issuer for three consecutive years (2022, 2023, and 2024).

with the HFCA Act.<sup>75</sup> In response to commenters opposed to implementing the trading prohibitions,<sup>76</sup> we point to the statutory mandate to impose trading prohibitions under the HFCA Act.<sup>77</sup> We agree with commenters<sup>78</sup> that a clear and transparent process for implementing and terminating a trading prohibition, and advance notice of such process, will assist market participants, minimize disruptions to the investors, and help to maintain fair and orderly markets. Accordingly, we have determined that it is appropriate to notify issuers, investors, and other market participants of the procedures by which the Commission will impose an initial or subsequent trading prohibition and terminate an initial or subsequent trading prohibition, including how issuers may certify that they have or will retain a non-PCAOB-Identified Firm pursuant to Section 104(i)(3)(B) or (D) of the Sarbanes-Oxley Act.<sup>79</sup>

## **2. Process for Imposing a HFCA Act Trading Prohibition**

As an initial matter, we have set forth above a clear and transparent process for identifying Commission-Identified Issuers that provides issuers with an opportunity to dispute their status as a Commission-Identified Issuer.<sup>80</sup> In addition, the Commission has stated that it will publicly disclose on its website the list of Commission-Identified Issuers, the number of

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<sup>75</sup> See, e.g., Sarbanes-Oxley Act, Sections 104(i)(1)(B) (defining the term “non-inspection year” to mean a year “(i) during which the Commission identifies the covered issuer under paragraph (2)(A) with respect to every report described in subparagraph (A) filed by the covered issuer during that year; and (ii) that begins after the date of enactment of this subsection”) and 104(i)(3)(A) (requiring the Commission to impose a trading prohibition if the Commission determines a covered issuer has three consecutive non-inspection years).

<sup>76</sup> See *supra* note 73.

<sup>77</sup> See *supra* note 65.

<sup>78</sup> See *supra* note 69.

<sup>79</sup> We note that unlike other provisions of the HFCA Act, the Commission is not required to undertake rulemaking to implement the trading prohibitions of Section 104(i)(3) of the Sarbanes-Oxley Act. See, e.g., Section 104(i)(4) of the Sarbanes-Oxley Act (requiring the Commission to issue rules establishing the manner and form for an issuer to submit documentation that it is not owned or controlled by a government entity in a foreign jurisdiction).

<sup>80</sup> See *supra* Section II.E.

consecutive years that an issuer has been identified as a Commission-Identified Issuer, and the application of any prior trading prohibition to an issuer.<sup>81</sup> As a result, investors and market participants should have sufficient notice regarding whether a security that they hold or plan to hold is issued by a Commission-Identified Issuer and of the risk that such security may be subject to a trading prohibition in the future, including the timeline for implementation of such trading prohibition if the issuer remains a Commission-Identified Issuer. Furthermore, an initial trading prohibition would not be imposed until an issuer has been a Commission-Identified Issuer for three consecutive years. Thus, issuers will have a period of three years to retain a non-PCAOB-Identified Firm before an initial trading prohibition would be imposed, and investors would have the same period of time in which to determine what action, if any, to take regarding their investments in any Commission-Identified Issuer.

Given the procedural protections afforded to issuers pursuant to the Commission’s approach provided herein and the fact that issuers and the investing public will have had sufficient notice of an issuer’s status as a Commission-Identified Issuer over a period of three years, we believe that it is appropriate and consistent with the protection of investors for the Commission to impose an initial trading prohibition and issue an order prohibiting the trading of an issuer’s securities<sup>82</sup> on a national securities exchange and in the over-the-counter market as

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<sup>81</sup> *See id.*

<sup>82</sup> A commenter asked for clarification of the impact of a trading prohibition on derivative securities. *See* letter from NYSE. The Sarbanes-Oxley Act, as amended by the HFCA Act, states that the Commission “shall prohibit *the securities of the covered issuer* from being traded . . . .” Section 104(i)(3)(A) of the Sarbanes-Oxley Act (emphasis added). Accordingly, to the extent the derivative security is issued by the Commission-Identified Issuer subject to the trading prohibition, that derivative security would also be subject to the trading prohibition. For example, if a Commission-Identified Issuer that is subject to a trading prohibition has issued equity securities and warrants on such equity securities, both the equity securities and the warrants would be prohibited from trading. However, we understand that most exchange-traded standardized equity options are issued by the Options Clearing Corporation, rather than the issuer of the underlying equity. *See, e.g.*, Financial Industry Regulatory Authority Rule 2360(a)(32) (defining “standardized equity option”). As another example, we understand that security-based swaps are generally entered into bilaterally between security-based swap

soon as practicable after the issuer has been determined to be a Commission-Identified Issuer for three consecutive years.<sup>83</sup>

An order issuing an initial trading prohibition would provide that such trading prohibition will be effective on the fourth business day after the order is published by the Commission.<sup>84</sup> We believe that providing a short delay in effectiveness of an initial trading prohibition appropriately addresses concerns regarding the risk to investors in U.S. markets of continued trading of Commission-Identified Issuers while also providing appropriate notice to investors and other market participants in order to make investment decisions. Moreover, the Commission believes this procedure will inform investors when a trading prohibition will be imposed and when it will become effective.<sup>85</sup>

Similarly, with respect to the imposition of a subsequent trading prohibition, the Commission would issue an order prohibiting the trading of an issuer's securities on a national securities exchange and in the over-the-counter market as soon as practicable after the issuer is

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dealers and/or eligible contract participants and are not issued by the issuer of the underlying equity securities. *See Treatment of Certain Communications Involving Security-Based Swaps That May Be Purchased Only by Eligible Contract Participants*, Release No. 33-10450 (Jan. 5, 2018) [83 FR 2046, 2051 n.60 (Jan. 16, 2018)] However, we further note that the imposition of a trading prohibition with respect to the underlying security of a derivative may itself have an impact on the derivative security, apart from the requirements of the Sarbanes-Oxley Act. And while this commenter requested the Commission to establish the impact of the trading prohibitions on any other securities market activities, such as clearance and settlement and options exercise and assignment, we note that there are already rules and processes in place in the securities markets to address when an equity security is subject to a trading halt, and those processes would generally apply with respect to a trading prohibition the same as they would with respect to any other trading halt. *See, e.g.*, Chicago Board Options Exchange Rules 4.4 (Withdrawal of Approval of Underlying Securities) and 502 (Trading Halts); Options Clearing Corporation Information Memo #30049 (Review of Trading Halt Processing).

<sup>83</sup> Those interested in providing feedback or discussing issues that may arise as a result of an initial trading prohibition or a subsequent trading prohibition may contact the Commission at the email address that will be provided on the [www.sec.gov/HFCAA](http://www.sec.gov/HFCAA) website.

<sup>84</sup> For example, if an order issuing a trading prohibition is published by the Commission on a Monday, the trading prohibition would be effective starting at 12:00 am (Washington D.C. time) the Friday of that week.

<sup>85</sup> While the HFCA Act does not address the delisting of securities from a national securities exchange, the existing rules of national securities exchanges that list issuers that are subject to an initial trading prohibition are applicable to delisting of such issuers' securities, as appropriate.

again identified as a Commission-Identified Issuer. An order issuing a subsequent trading prohibition would provide that the trading prohibition will be effective on the fourth business day after the order is published by the Commission.<sup>86</sup> As with the process for issuing an initial trading prohibition, we believe that this procedure appropriately addresses concerns regarding the risk to investors in U.S. markets of continued trading of Commission-Identified Issuers that have previously been subject to an initial trading prohibition while also providing appropriate notice to investors and other market participants in order to make investment decisions. We believe that the application of a prior trading prohibition, the ability of an issuer to dispute its status as a Commission-Identified Issuer, the public availability of the provisional list of Commission-Identified Issuers,<sup>87</sup> and an issuer's repeat use of a registered public accounting firm that the PCAOB is unable to inspect or investigate completely warrant the same short delay in the effectiveness of a subsequent trading prohibition as in an initial trading prohibition. In addition, we believe this procedure will inform investors when a subsequent trading prohibition will be imposed and become effective.<sup>88</sup>

### **3. Process for Terminating Trading Prohibitions; Required Certification**

Section 104(i)(3)(B) of the Sarbanes-Oxley Act provides that the Commission shall terminate an initial trading prohibition if a Commission-Identified Issuer certifies to the Commission that the issuer has retained a registered public accounting firm that the PCAOB has

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<sup>86</sup> See *supra* note 84.

<sup>87</sup> We note that a provisional list of issuers that may be identified as Commission-Identified Issuers will be made publicly available before it is finalized. Accordingly, investors and other market participants would have access to the provisional list and would therefore have notice that a subsequent trading prohibition may be forthcoming. See *supra* Section II.E.

<sup>88</sup> While the HFCA Act does not address the delisting of securities from a national securities exchange, the existing rules of national securities exchanges that list issuers that are subject to a subsequent trading prohibition are applicable to delisting of such issuers' securities, as appropriate.

inspected to the satisfaction of the Commission.<sup>89</sup> Section 104(i)(3)(D) of the Sarbanes-Oxley Act also provides that the Commission shall terminate a subsequent trading prohibition if the Commission-Identified Issuer certifies to the Commission that the issuer will retain a registered public accounting firm that the PCAOB is able to inspect under this section.<sup>90</sup>

As a general matter, the retention of a registered public accounting firm does not guarantee that the newly engaged accounting firm will be the firm that issues an audit report on the financial statements of the issuer. Specifically, an issuer could retain more than one audit firm or retain a non-PCAOB-Identified Firm and subsequently replace the non-PCAOB-Identified Firm with a PCAOB-Identified Firm. Thus, in order to achieve the result that the retained non-PCAOB-Identified Firm is actually performing the audit, we believe it appropriate and consistent with the protection of investors that, for a Commission-Identified Issuer to certify consistent with Section 104(i)(3)(B) of the Sarbanes-Oxley Act, a Commission-Identified Issuer must file financial statements that include an audit report signed by a non-PCAOB-Identified Firm. Such a certification made by a Commission-Identified Issuer subject to an initial trading prohibition will terminate an initial trading prohibition.

Accordingly, a Commission-Identified Issuer subject to an initial trading prohibition can make the required certification that it “has retained” a non-PCAOB-Identified Firm to the satisfaction of the Commission only if such certification is preceded or accompanied by the filing of an annual report or an amended annual report with financial statements that include an audit report on the consolidated financial statements signed by a non-PCAOB-Identified Firm. We believe that lifting the trading prohibition prior to the Commission-Identified Issuer filing

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<sup>89</sup> See Section 104(i)(3)(B) of the Sarbanes-Oxley Act.

<sup>90</sup> See Section 104(i)(3)(D) of the Sarbanes-Oxley Act.

financial statements that include such an audit report would place investors at risk by commencing trading in a security for which the latest three annual reports filed with the Commission are audited by a PCAOB-Identified Firm. In addition, lifting the trading prohibition prior to the issuer filing financial statements that include an audit report on the consolidated financial statements signed by a non-PCAOB-Identified Firm could place investors at risk by commencing trading in a security that could potentially become subject to a subsequent trading prohibition lasting a minimum of five years if the issuer does in fact use a PCAOB-Identified Firm to perform its audit for its next annual report. Therefore, we believe it would be appropriate to terminate an initial trading prohibition only after investors and regulators have access to financial statements that include an audit report on the consolidated financial statements signed by a non-PCAOB-Identified Firm.

Similarly, we believe that a Commission-Identified Issuer that is subject to a subsequent trading prohibition should make at least the same showing to end trading prohibition as a Commission-Identified Issuer that is subject to an initial trading prohibition. Accordingly, for a Commission-Identified Issuer to certify consistent with Section 104(i)(3)(D) of the Sarbanes-Oxley Act, a Commission-Identified Issuer must file, either with or prior to its certification, an annual report or amended annual report with financial statements that include an audit report signed by a non-PCAOB-Identified Firm. Such a certification made by a Commission-Identified Issuer subject to a subsequent trading prohibition will terminate a subsequent trading prohibition.<sup>91</sup> We believe that the concerns described above with respect to an initial trading prohibition are even greater with Commission-Identified Issuers subject to a subsequent trading

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<sup>91</sup> The certification could be signed by any individual that is duly authorized to execute and deliver such a certification on behalf of the Commission-Identified Issuer.

prohibition as a result of a repeated reliance on a PCAOB-Identified Firm. Further, an issuer subject to a subsequent trading prohibition would have at least five years to retain a non-PCAOB-Identified Firm to audit its financials before a subsequent trading prohibition could be terminated by the Commission.

As described above, a Commission-Identified Issuer subject to an initial or subsequent trading prohibition must certify that it has or will retain a non-PCAOB-Identified Firm for the Commission to end a trading prohibition,<sup>92</sup> and such certification would be submitted at the same time as, or after, the issuer files an annual or amended annual report with financial statements that include an audit report signed by a non-PCAOB-Identified Firm.<sup>93</sup> Once the Commission receives the certification and has verified that the issuer has in fact filed an annual or amended annual report with financial statements that include an audit report signed by a non-PCAOB-Identified Firm, the Commission shall as soon as practicable issue an order ending the initial or subsequent trading prohibition, as the case may be. An order ending an initial or subsequent trading prohibition will provide that the termination of the trading prohibition will be effective the next business day after the order is published by the Commission. We believe that once an issuer has certified to the satisfaction of the Commission that it has retained a non-PCAOB-Identified Firm, termination of the trading prohibition should not be delayed.

#### **G. Amendment to the Delegations of Authority of the Commission**

The Commission is adopting new Rule 30-1(m) that delegates Commission authority to the Director of the Division of Corporation Finance to identify a registrant as a Commission-

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<sup>92</sup> See Sections 104(i)(3)(B) and (D) of the Sarbanes-Oxley Act. Section 104(i)(3)(D) of the Sarbanes-Oxley Act further provides that, with respect to a subsequent trading prohibition, the issuer may not submit such certification until after the end of the five-year period.

<sup>93</sup> Any certification should be submitted in accordance with the EDGAR Filer Manual.

Identified Issuer. This delegated authority is designed to conserve Commission resources by permitting Commission staff to carry out the procedures described herein in connection with the identification of Commission-Identified Issuers. The Commission staff may nevertheless submit matters to the Commission for consideration, as it deems appropriate.

### **III. Procedural and Other Matters**

If any of the provisions of these rules, or the application thereof to any person or circumstance, is held to be invalid, such invalidity shall not affect other provisions or application of such provisions to other persons or circumstances that can be given effect without the invalid provision or application.

Pursuant to the Congressional Review Act, the Office of Information and Regulatory Affairs has designated these rules as not a “major rule,” as defined by 5 U.S.C. 804(2).

The Administrative Procedure Act (“APA”) generally requires an agency to publish notice of a rulemaking in the Federal Register and provide an opportunity for public comment. This requirement does not apply, however, if the agency “for good cause finds . . . that notice and public procedure are impracticable, unnecessary, or contrary to the public interest.” Section 2 of the HFCA Act requires Commission rulemaking within 90 days of the date of enactment in order to “establish the manner and form in which a covered issuer shall make a submission required under paragraph (2)(B).” Furthermore, Section 3 of the HFCA Act requires certain disclosure from issuers, and the amendments to Form 10-K, Form 20-F, Form 40-F, and Form N-CSR clarify issuers’ obligations under the HFCA Act. Because the interim final amendments conformed the specified forms to the requirements of a newly enacted statute and in light of the 90- day rulemaking directive in Section 2 of the HFCA Act, the Commission found in the

Interim Final Release that notice and public comment were impracticable and unnecessary.<sup>94</sup>

The revisions to the interim final amendments being adopted in this release are in response to feedback received on requests for comment in the Interim Final Release.

#### **IV. Economic Analysis**

##### **A. Introduction and Broad Economic Considerations**

As discussed above, we are finalizing amendments to Form 10-K, Form 20-F, Form 40-F, and Form N-CSR that implemented the disclosure and submission requirements of the HFCA Act. We are mindful of the costs imposed by, and the benefits obtained from, our rules. In this section, we analyze potential economic effects stemming from the amendments.<sup>95</sup> We analyze these effects against a baseline that consists of the current regulatory framework and current market practices.

We are finalizing the interim final amendments with a modification to clarify that a Commission-Identified Foreign Issuer listed in the United States using VIE or any structure that results in additional foreign entities being consolidated in the financial statements of the

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<sup>94</sup> Accordingly, the interim final amendments did not require a final regulatory flexibility analysis under the Regulatory Flexibility Act. *See* 5 U.S.C. 604(a) (requiring a final regulatory flexibility analysis only for rules required by the APA or other law to publish a general notice of proposed rulemaking). For the same reason, these amendments do not require a final regulatory flexibility analysis).

<sup>95</sup> Exchange Act Section 3(f) requires the Commission, when engaging in rulemaking where it is required to consider or determine whether an action is necessary or appropriate in the public interest, to consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation. Further, Exchange Act Section 23(a)(2) requires the Commission, when making rules under the Exchange Act, to consider the impact that the rules would have on competition and prohibits the Commission from adopting any rule that would impose a burden on competition that is not necessary or appropriate in furtherance of the purposes of the Exchange Act. Additionally, Section 2(c) of the Investment Company Act requires us, when engaging in rulemaking that requires us to consider or determine whether an action is consistent with the public interest, to also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation. Although we are adopting amendments to Form N-CSR to implement the HFCA Act as applied to registered investment companies, based on recent Form N-CEN filings, no registered investment company reported having retained a registered public accounting firm located in a foreign jurisdiction for the preparation of the company's financial statements. Based on this data, and Commission staff experience, we estimate that no registered investment companies will be subject to the requirements of the interim final amendments upon the rule's adoption. Accordingly, we do not expect any economic effects associated with the amendment to Form N-CSR.

registrant, must provide the HFCA Act's required disclosures regarding government ownership of shares of the operating company. We also are adding a requirement for registrants to tag the name, jurisdiction, and the PCAOB ID Number(s) of the audit firm(s) that sign the audit report accompanying a registrant's Form 10-K, Form 20-F, and Form 40-F. In this economic analysis, we discuss the economic effects arising from the interim final amendments as finalized, including the modifications discussion above. Where possible, we have attempted to quantify the expected economic effects of the amendments. Some of the potential economic effects are inherently difficult to quantify. In some instances, we lack the information or data necessary to provide reasonable estimates for the economic effects of the amendments. Where we cannot quantify the relevant economic effects, we discuss them in qualitative terms.

The new disclosure requirements will increase transparency about the reliability of affected issuers' financial statements as well as the characteristics of their ownership and control structures. High-quality disclosures, including high-quality financial statements, are a cornerstone of well-functioning capital markets.<sup>96</sup> Such disclosures reduce information asymmetries between investors and issuers, with positive effects on price efficiency and capital allocation.<sup>97</sup> Broadly speaking, academic research shows that increasing the quality of financial reporting improves price efficiency and reduces an issuer's cost of capital.<sup>98</sup>

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<sup>96</sup> See, e.g., Christian Leuz & Peter Wysocki, *The Economics of Disclosure and Financial Reporting Regulation*, 54 J. ACCT. RESEARCH 525 (2016); and Anne Beyer, Daniel Cohen, Thomas Lys & Beverly Walther, *The Financial Reporting Environment: Review of the Recent Literature*, 50 J. ACCT. ECON 296 (2010).

<sup>97</sup> See, e.g., Douglas W. Diamond & Robert E. Verrecchia, *Disclosure, Liquidity, and the Cost of Capital*, 46 J. FIN. 1325 (1991).

<sup>98</sup> See, e.g., Stephen Brown & Stephen A. Hillegeist, *How Disclosure Quality Affects the Level of Information Asymmetry*, 12 REV. ACCOUNT. STUD. 443 (2007) (showing how better disclosure quality reduces information asymmetry); Nilabhra Bhattacharya, Hemang Desai, & Kumar Venkataraman, *Does Earnings Quality Affect Information Asymmetry? Evidence from Trading Costs*, 30 CONT. ACCOUNT. RES. 482 (2013) (showing that earnings quality reduces information asymmetry); Partha Sengupta, *Corporate Disclosure Quality and the Cost of Debt*, 73 ACCOUNT. REV. 459 (1998) (showing that high disclosure quality reduces the cost of debt); Christine Botosan, *Disclosure Level and the Cost of Equity Capital*, 72 ACC. REV. 323 (1997) (finding that

Financial reporting quality is in part determined by audit quality. According to some academic studies, PCAOB oversight has led to improvements in audit quality and to increased investor confidence in the quality of the audited financial statements.<sup>99</sup> However, when the PCAOB is unable to inspect some auditors there is a lack of transparency with respect to the audit quality provided by such firms. As a result, there may be uncertainty regarding the reliability of the financial information of issuers audited by firms that are not inspected, which can potentially lead to suboptimal investment decisions by investors.

In addition, academic literature provides evidence of varying types of impact of ownership and control structures on firm value.<sup>100</sup> Government ownership, in particular, can be related to both risks and benefits for investors. Evidence in the literature highlights inefficiencies and expropriation risks as a result of government ownership or control, whereas other studies provide evidence of easier access to financing.<sup>101</sup> Effects from government

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disclosure quality reduces the cost of equity for firms with low analyst coverage); Mark E. Evans, *Commitment and Cost of Equity Capital: An Examination of Timely Balance Sheet Disclosure in Earnings Announcements*, 33 CONT. ACCOUNT. RES. 1136 (2016) (finding that “firms which consistently disclose balance sheet detail in relatively timely earnings announcements have lower costs of capital compared to other firms”); For a survey of financial reporting research, see Anne Beyer, Daniel A. Cohen, Thomas Z. Lys, & Beverly R. Walther, *The Financial Reporting Environment: Review of the Recent Literature*, 50 J. ACCOUNT. ECON. 296 (2010).

<sup>99</sup> See, e.g., Daniel Aobdia, *The Impact of the PCAOB Individual Engagement Inspection Process—Preliminary Evidence*, 93 ACCOUNT. REV. 53 (2018) (concluding that “both audit firms and clients care about the PCAOB individual engagement inspection process and, in several instances, gravitate toward the level set by the Part I Finding bar”); Mark L. DeFond & Clive S. Lennox, *Do PCAOB Inspections Improve the Quality of Internal Control Audits?*, 55 J. ACCOUNT. RES. 591 (2017) (finding evidence consistent with “PCAOB inspections improving the quality of internal control audits by prompting auditors to remediate deficiencies in their audits of internal controls”); Brandon Gipper, Christian Leuz, & Mark Maffett, *Public Oversight and Reporting Credibility: Evidence from the PCAOB Audit Inspection Regime*, 33 REV. FINANC. STUD. 4532 (concluding that “consistent with an increase in reporting credibility after the introduction of public audit oversight, we find that capital market responses to earnings surprises increase significantly”).

<sup>100</sup> See, e.g., Andrei Shleifer & Robert Vishny, *A Survey of Corporate Governance*, 52 J. FIN. 737 (1997) (discussing both the theory and empirical evidence on the effect of large shareholders on firm value).

<sup>101</sup> See, e.g., Ginka Borisova, Veljko Fotak, Kateryna Holland & William Megginson, *Government Ownership and the Cost of Debt: Evidence from Government Investments in Publicly Traded Firms*, 118 J. FIN. ECON. 168 (2015) (showing that during times of firm-specific or economy-wide distress, the dominant effect of state equity ownership is a reduction in the cost of debt, consistent with an implicit debt guarantee of government ownership); Gongmen Chen, Michael Firth & Liping Xu, *Does the Type of Ownership Control Matter?*

ownership or control on firm value may be further amplified when the regulatory environment in the foreign jurisdiction is weak, and when there is heightened political risk.<sup>102</sup>

The required disclosures and submissions will reduce uncertainty about characteristics that may affect firm value and risk and therefore could facilitate investors' capital allocation decisions. Some of the information required to be disclosed under the amendments may be otherwise available to investors through other sources or overlap with existing mandated disclosures.<sup>103</sup> In such cases, we expect the required disclosures could nevertheless reduce search costs for investors and potentially enhance investor protection. In addition, the submission requirement will provide some reassurance to investors that Commission-Identified Issuers that do not disclose any ownership or control by governmental entities (in foreign jurisdictions that prevent PCAOB inspections) are not, in fact, owned or controlled by such entities.

The amendments will impose compliance costs on issuers that may vary based on characteristics of their audit arrangements and ownership structure. Although these compliance costs, in and of themselves, may not be significant for most firms, the costs may nonetheless cause certain issuers to accelerate their response to other aspects of the HFCA Act, such as switching audit firms or exiting the U.S. markets altogether. Those effects are likely to be much more significant than the comparatively limited benefits and costs associated with the interim

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*Evidence from China's Listed Companies*, 33 J. BANK. FINANCE 171 (2009) (finding evidence that the type of government ownership affects value and performance).

<sup>102</sup> See, e.g., Laura Liu, Haibing Shu & John Wei, *The Impacts of Political Uncertainty on Asset Prices: Evidence from the Bo Scandal in China*, 125 J. FIN. ECON. 286 (2017) (concluding that political uncertainty is a priced risk as evidenced by stock price reactions following the 2012 Bo Xilai political scandal in China; the study shows amplified effects on prices for state-owned enterprises and politically connected companies); Bryan Kelly, Lubos Pastor & Pietro Veronesi, *The Price of Political Uncertainty: Theory and Evidence from the Option Market*, 71 J. FIN. 2417 (2016) (finding that options whose lives span political events tend to be more expensive, and that such protection is more valuable in a weaker economy and amid higher political uncertainty).

<sup>103</sup> See *infra* Section IV.B.1.

final amendments.

## **B. Baseline**

### **1. Regulatory Baseline**

The regulatory baseline for these amendments includes the interim final amendments adopted on March 18, 2021, and the PCAOB Rule 6100, Board Determinations Under the Holding Foreign Companies Accountable Act, adopted the PCAOB on September 22, 2021 and approved by the Commission on November 4, 2021.<sup>104</sup>

The disclosures and submissions required by the amendments will provide the Commission, as well as market participants, with more readily accessible and comparable information regarding a number of Commission-Identified Issuers' characteristics, namely: (1) the extent of ownership or control by a governmental entity in a jurisdiction where the PCAOB is unable to inspect or investigate completely because of a position taken by an authority in that jurisdiction, (2) the use of a registered public accounting firm in preparation of an audit report that the PCAOB is unable to fully inspect, (3) the presence and identity of any official of the CCP who is a member of the board of directors, and (4) the presence and specific text of any charter of the CCP contained in the registrant's articles of incorporation (or equivalent organizing document). We therefore analyze the extent to which such requirements will change existing regulatory requirements or the current practices of potentially affected registrants.

Compliance with the HFCA Act will require disclosures and submissions pertaining to the ownership or control of a registrant by a governmental entity in the foreign jurisdiction of the registered public accounting firm that the PCAOB is unable to inspect or investigate completely. In practice, many registrants already include disclosures similar to the information required by

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<sup>104</sup> See *supra* note 10.

the HFCA Act in the portions of their respective periodic reports pertaining to registrant-specific risks.<sup>105</sup> Others provide detailed diagrams to illustrate their ownership structure within their descriptions of business or otherwise seek to inform readers of their VIE arrangements within the financial statements included in periodic disclosures.<sup>106</sup> The levels of detail and specificity associated with these disclosures vary, however, and the information often is not easily comparable across filings given that similar disclosures may not occur within the same item or section of the report.<sup>107</sup>

One notable exception to this variation in disclosures, however, is the disclosure by registrants of the PCAOB's inability to conduct inspections of their respective independent audit firms. We observe a highly similar type and pattern of disclosure regarding the PCAOB's inability to inspect those firms included in the majority of the potential Commission-Identified Issuers' Item 3 (for Form 20-F filers) and Item 1A (for Form 10-K filers) discussion of risk factors.<sup>108</sup> Such disclosures are readily accessible using the keyword search functionality on the

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<sup>105</sup> For example, some registrants may provide these disclosures in response to 17 CFR 229.105 (Item 105 of Regulation S-K) (requiring a registrant to disclose a discussion of the material factors that make an investment in the registrant or offering speculative or risky).

<sup>106</sup> See Financial Accounting Standards Board Interpretation No. 46, Consolidation of Variable Interest Entities.

<sup>107</sup> See, e.g., Justin Hopkins, Mark H. Lang & Jianxin (Donny) Zhao, *The Rise of US-Listed VIEs from China: Balancing State Control and Access to Foreign Capital*, Darden Business School (Working Paper No. 3119912), Kenan Institute of Private Enterprise Research Paper No. 19-17 (2018), available at <http://dx.doi.org/10.2139/ssrn.3119912> (finding that, Chinese firms disclose using a VIE structure in 42 percent of reviewed year 2013 Forms 10-K, where "some firms simply mention the VIE structure in passing, while others explicitly disclose the legal risks of the VIE, documenting which specific subsidiaries utilize the VIE and provide pro forma balance sheets and income statements for these subsidiaries, as well as summarizing the specific contracts including the parties and terms"). See also, Paul Gillis & Michelle R. Lowry, *Son of Enron: Investors Weigh the Risks of Chinese variable Interest Entities*, 26 J. APPL. CORP. FIN. 61 (2014).

<sup>108</sup> Staff conducted a review of annual report disclosures using a combination of Intelligize searches and a manual review of select filings of Forms 10-K and 20-F. Highly similar language describing the potential risks associated with the PCAOB's inability to conduct inspections appeared across at least 65% of annual reports filed within the same year, including reviewed periods that predate the initial introduction of the HFCA Act legislation in 2019. As no single audit firm currently serves more than, at maximum, 20% of potential Commission-Identified Issuers, the inclusion of standard disclosures across registrants does not appear to be

Commission’s EDGAR website.<sup>109</sup> In addition, similar identification of registrants whose independent auditors were not fully inspected by the PCAOB due to limitations and restrictions imposed by authorities in foreign jurisdictions has historically been available via the PCAOB’s dedicated “Public Companies that are Audit Clients of PCAOB-Registered Firms from Non-U.S. Jurisdictions where the PCAOB is Denied Access to Conduct Inspections” webpage.<sup>110</sup>

Under the amendments, Commission-Identified Foreign Issuers will also be required to disclose the presence and identity of any official of the CCP who is a member of its board of directors in addition to the percentage of the shares of the issuer owned by governmental entities in the foreign jurisdiction in which the issuer is incorporated or otherwise organized and whether governmental entities in the applicable foreign jurisdiction with respect to that registered public accounting firm have a controlling financial interest with respect to the issuer. At present, some of this information may be elicited by Form 10-K disclosure requirements<sup>111</sup> or Form 20-F disclosure requirements.<sup>112</sup> Because Form 10-K, Part III disclosures may be incorporated by reference from the registrant’s definitive proxy statement if filed within 120 days of the related

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attributable to the practices of any individual audit firm. *See infra* note 117 for a description of the sample identification methodology.

<sup>109</sup> Available at <https://www.sec.gov/edgar/search/>.

<sup>110</sup> Available at <https://pcaobus.org/oversight/international/denied-access-to-inspections>.

<sup>111</sup> *See* 17 CFR 229.401 (Item 401 of Regulation S-K), 17 CFR 229.403 (Item 403 of Regulation S-K), and 17 CFR 229.404 (Item 404 of Regulation S-K), required under Items 10, 12 and 13 of Form 10-K. Item 401 of Regulation S-K requires disclosure relating to the identification of directors and a brief description of their business experience. Item 403 of Regulation S-K requires disclosure with respect to any person or group that beneficially owns more than five percent of any class of the registrant’s voting securities, as well as ownership information of executive officers and directors of the registrant. Item 404 of Regulation S-K requires disclosure of transactions between the registrant and related persons, such as officers, directors and significant shareholders.

<sup>112</sup> *See* Items 6 and 7 of Form 20-F. Item 6 of Form 20-F requires disclosure relating to the identification and share ownership of directors and senior management. Item 7 of Form 20-F requires disclosure with respect to beneficial owners of more than five percent of any class of the registrant’s voting securities, disclosure with respect to related party transactions, as well as disclosure of whether the company is directly or indirectly owned or controlled by another corporation or foreign government and the nature of that control.

Form 10-K fiscal year end, or alternatively filed as a Form 10-K amendment by the same 120 day deadline, such disclosures are not currently uniformly present in the annual report filings of the potentially affected issuers. Moreover, there are currently no requirements that such disclosures must include the political party affiliation or party posts of those responsible for registrants' management and oversight, including but not limited to members of the board. Nor is there a requirement to systematically disclose the identity and ownership stake of any person or group of persons – including government entities – who directly or indirectly acquire or have beneficial ownership of less than five percent of a class of a Commission-Identified Issuer's securities.

Finally, under the amendments, Commission-Identified Foreign Issuers will be required to state whether the articles of incorporation of the issuer (or equivalent organizing document) contains any charter of the CCP, including the text of any such charter. While periodic reporting requirements currently instruct registrants to include a complete copy of the articles of incorporation and bylaws as an exhibit to the annual report,<sup>113</sup> there are no requirements to identify the political or textual origins of any portion of a registrant's articles of incorporation. In practice, given that a registrant may simply indicate in its annual report exhibit index that such articles are incorporated by reference,<sup>114</sup> few filers include the full text of such articles, bylaws, or charters in annual report filings after initially doing so at the time of initial public offering ("IPO") registration. Similarly, amended or revised versions of the registrant's articles of incorporation and bylaws are generally not included in the annual report filing, but are incorporated by reference as well. In these cases, locating the submission to which the

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<sup>113</sup> See Item 19, Instruction 1 of Form 20-F and 17 CFR 229.601(b)(3)(i).

<sup>114</sup> See 17 CFR 240.12b-23(c).

registrant's complete and most recent version of its articles of incorporation are attached in their entirety requires a search and review of the registrant's current reports (on Forms 8-K or 6-K).<sup>115</sup> Therefore, under current regulatory requirements and in practice, the majority of annual reports filed by potential Commission-Identified Foreign Issuers do not include, either in part or in complete form, the registrant's articles of incorporation, from which the reader might assess the presence or absence of text from the charter of the CCP.

## **2. Affected Parties**<sup>116</sup>

### **a. Registrants**

Registrants subject to periodic reporting requirements under the Exchange Act will not be affected by the amendments unless and until they are Commission-Identified Issuers. Commission identification of such issuers is in turn contingent upon initial identification of affected registered public accounting firms that are retained by registrants with periodic disclosure obligations. Based upon a review of such registrants in calendar year 2020, we identified 273 registrants for whom future identification as a Commission-Identified Issuer might occur, based on current facts and circumstances.<sup>117</sup> Of these potential Commission-Identified

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<sup>115</sup> The requirement to submit a Form 6-K in such cases by registrants that use Form 20-F to file annual reports depends upon the current reporting requirements of the relevant foreign jurisdiction. Because potential Commission-Identified Issuers domiciled, incorporated, or organized in China are required by Chapter 5 Article 27 of the Regulations of the People's Republic of China on Administration of Company Registration to file a complete copy of the revised articles within 30 days of such changes, a similar requirement to promptly furnish a Form 6-K including the complete revised articles of incorporation also applies. This document may then be incorporated by reference in the registrant's subsequent annual reports. Analogous requirements for registrants using domestic forms are outlined in Form 8-K, Item 5.03.

<sup>116</sup> As noted above, the amendments may accelerate responses to other aspects of the HFCA Act, such as switching audit firms or exiting the U.S. markets altogether. These responses could impact parties beyond those identified below (*e.g.*, audit firms). For purposes of this economic analysis, we focus on those parties affected by the interim final amendments.

<sup>117</sup> Analysis is based on staff review of data obtained from the PCAOB (*see supra* note 110108), Audit Analytics, manual review of all annual reports filed by foreign issuers using Forms 20-F, 40-F, or an amendment thereto in calendar year 2020, and review of securities registered in calendar year 2020 by foreign issuers. This analysis

Issuers candidates, 18.2 percent filed annual disclosures using Form 10-K while 78.2 percent are Form 20-F filers. No filings submitted by potential candidates were made using Forms 40-F or N-CSR. Among filers, approximately 22 percent were incorporated in the United States while 78 percent were incorporated in foreign jurisdictions, including 4.8 percent who self-disclosed to be state-owned enterprises. These registrants' securities either are listed on a national exchange (88.7 percent), OTC-listed (9.9 percent), or report no U.S. listing (1.5 percent).<sup>118</sup> Of the 273 Commission-Identified Issuers, five are listed in the Annex to Executive Order 14032 as issuers that are affiliated with the Chinese military.<sup>119</sup> Additionally, a recent study found that 42 percent of US-listed Chinese firms disclosed using a VIE structure in year 2013.<sup>120</sup>

## **b. Investors**

The amendments may impact both current investors in affected registrants as well as potential investors that may consider investing in these registrants in the future. As mentioned

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may potentially be viewed as an upper bound on the future number of registrants that may be affected by the HFCA requirements as clients of those firms previously identified by the PCAOB.

<sup>118</sup> Using a more conservative approach that looked only to registrants with at least one annual report filed after the introduction of the HFCA Act, we further estimate that in calendar year 2020, 194 registrants submitted an annual report (Form 10-K, 20-F, or an amendment) whose auditor was previously identified by the PCAOB (*see supra* note 110) as a registered firm from a non-U.S. jurisdiction where necessary access to conduct oversight was denied due to a position taken by local authorities. Based on our historical analysis of these registrants, 18 percent submitted annual reports using a domestic form, while 82 percent and zero percent submitted their annual reports via foreign filings Form 20-F and Form 40-F, respectively. Based on the same population of registrants, we estimate that approximately three percent of potentially affected registrants disclosed their securities as listed on two or more foreign exchanges, approximately nine percent listed on only one foreign exchange, while approximately 79 percent only disclosed listing on a U.S. national exchange. Of these registrants, 13 (equal to six percent) self-identified in their 2020 disclosures as state-owned enterprises.

<sup>119</sup> Executive Order 14032, titled "Addressing the Threat From Securities Investments That Finance Certain Companies of the People's Republic of China," was signed by United States President Joe Biden on June 3, 2021, and came into effect on August 2, 2021 [86 FR 30145 (June 7, 2021)]. It generally prohibits U.S. persons from purchasing or selling securities of issuers identified as Communist Chinese Military-Industrial Companies. The annex to the Executive order includes a list of such companies as determined by the US Treasury.

<sup>120</sup> Justin Hopkins, Mark H. Lang & Jianxin (Donny) Zhao, *The Rise of US-Listed VIEs from China: Balancing State Control and Access to Foreign Capital*, Darden Business School Working Paper No. 3119912, Kenan Institute of Private Enterprise Research Paper No. 19-17 (2018), available at <http://dx.doi.org/10.2139/ssrn.3119912>.

above, at least some of the information elicited by the required disclosures is likely to be available already to investors through various existing channels, such as vendor databases or various third-party reports, but at varying costs. As such, we expect that the required disclosures are likely to affect mostly retail investors who directly invest or consider investing in affected registrants since it may be more costly for these investors to obtain such information absent the required disclosures. Institutional or other sophisticated investors may also be impacted by the amendments; however, we expect that such impact might be limited given their resources to obtain the required information from other sources (*e.g.*, vendor databases), when such sources are available.

### **C. Economic Effects**

#### **1. Benefits and Costs of HFCA Act Disclosure Requirements**

For Commission-Identified Foreign Issuers, the amendments will require specific disclosures to be made in these registrants' annual reports.<sup>121</sup> In general, as discussed above, the required disclosures elicit information that some academic literature has found is value-relevant to investors. As such, we expect the required disclosures to be beneficial to investors because they are likely to reduce search costs when the information in the required disclosure is otherwise available through diverse sources or existing disclosures, and also potentially provide investors with information about aspects of these registrants' governance characteristics that otherwise might not be available or relatively costly to obtain. We do not expect significant compliance costs for Commission-Identified Foreign Issuers given that these registrants likely already possess the information required by the amendment; however, registrants may incur

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<sup>121</sup> *See supra* Section II.B for a detailed description of the disclosure requirements mandated by Section 3 of the HFCA Act.

additional compliance costs if the required information is not readily accessible to them or needs to be formatted for the required disclosure.

**a. Investors**

The amendments will require disclosure that a registered public accounting firm that the PCAOB is unable to inspect or investigate completely because of a position taken by an authority in the foreign jurisdiction has issued an audit report for the registrant. The disclosure will provide transparency about the inspection status of the engaged audit firm. As discussed above, the academic literature provides evidence that the PCAOB's oversight has led to improvements in audit quality and financial reporting quality, for both domestic and foreign issuers. The inability of the PCAOB to inspect the auditors of these registrants could generate uncertainty regarding their financial reporting quality. Thus, to the extent this information is new to investors,<sup>122</sup> we expect the specific required disclosure to potentially facilitate investors' capital allocation decisions. We further expect that the presentation of such information in a standardized form in the annual report is likely to be helpful to investors by reducing their search costs.

The amendments will require disclosure of the percentage of the shares of the registrant owned by a government entity in the foreign jurisdiction. As discussed above, government ownership is information that is likely relevant to investors' capital allocation decisions. For example, disclosure of government ownership may allow investors to better assess potential political risks/effects related to government ownership in the foreign jurisdiction that may influence the value of their investment. These benefits would be limited to the extent that

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<sup>122</sup> See *supra* Section IV.B.1 for a description of current practice and regulatory requirements regarding disclosure of the registrant's auditor inspection status.

affected registrants already provide disclosure relevant to assessing such risks.

In addition to the disclosure of ownership through equity holdings, the amendments will require affected registrants to disclose whether a governmental entity has a controlling financial interest in the registrant. We expect such disclosure may benefit investors as it could provide information about other mechanisms, besides direct equity ownership, such as control through a pyramidal ownership structure that might allow a governmental entity to influence registrants' operational and other decisions. This information would provide additional insight into potential risks to investors that might arise from such control/ownership structures.<sup>123</sup> One commenter agreed that such disclosure will be informative for investors.<sup>124</sup>

The amendments also require disclosure of board members' affiliations with the CCP and whether the articles of incorporation of the registrant (or equivalent organizing document) includes any charter of the CCP, including the text of any such charter. These disclosures will enhance existing information on the composition of the board and could increase insight into its quality and the related consequences for firm value. One study shows that the degree of a board's political affiliation in China is related to firm value, and this varies based on facts and circumstances.<sup>125</sup> For example, political affiliation of board members may imply that their incentives may not align with shareholders' interests. Under different circumstances, politically-

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<sup>123</sup> See, e.g., Jesse Fried & Ehud Kamar, *Alibaba: A Case Study of Synthetic Control*, European Corporate Governance Institute Working Paper Series in Law, Paper No 533/2020 (2020) (concluding that control of a firm can be exerted not only through equity, but through a mixture of employment, contractual, and commercial arrangements).

<sup>124</sup> See letter from ASA.

<sup>125</sup> See Lihong Wang, *Protection or Expropriation: Politically Connected Independent Directors in China*, 55 J. BANK. FIN. 92 (2015) (using a sample of Chinese listed firms over the 2003-2012 period, the study finds that while the presence of politically connected independent directors is related to increased firm value for private firms, the presence of politically connected independent directors is related to lower firm value for state-owned enterprises ("SOEs"). The study also finds an increase in related-party transactions for Chinese listed firms with politically connected independent directors).

connected board members may facilitate the execution of financing transactions for the registrant. To the extent that these disclosures may benefit investors by facilitating their efforts to evaluate characteristics of registrants that may have an impact on the value of their investments, these specific disclosures may facilitate investors' capital allocation decisions and potentially increase investor protection.

In a modification to the interim final rule, the final rules will specify that the registrant must look through a VIE or any structure that results in additional foreign entities being consolidated in the financial statements of the registrant and provide disclosure about the operating company in the relevant jurisdiction. Thus, any Commission-Identified Foreign Issuer that uses a VIE or other similar corporate structure will be required to provide the required disclosures for itself and its foreign operating entity. This change will benefit investors by providing more accurate information regarding the true ownership structure of Commission-Identified Foreign Issuers. One commenter suggested that a VIE structure could block meaningful disclosure of financial and political information.<sup>126</sup>

In another change from the interim final rule, the final amendments will include a new Inline XBRL tagging requirement: registrants will have to tag the auditor name, jurisdiction, and the PCAOB ID Number(s) of the audit firm(s) that appear on the audit report signed by the registered public accounting firm in the registrant's Form 10-K, Form 20-F, and Form 40-F. Such tagging requirement will likely benefit investors by providing them with machine-readable information on auditors directly from a registrant's annual report, thus allowing them to identify registrants with auditors from jurisdictions that do not allow PCAOB oversight. This change will also facilitate the Commission's accurate and efficient identification of Commission-

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<sup>126</sup> See letter from Kelly.

Identified Issuers. Since registrants already use Inline XBRL tagging in their annual reports and other filings with the commission, and the information on auditor name and jurisdiction is readily available to them, we do not believe this change will result in a significant cost increase for them.

### **b. Registrants**

The required disclosures are likely to impose some compliance costs on Commission-Identified Foreign Issuers. One commenter asserted that the proposed disclosures were repetitive of disclosure that is already provided and would result in unnecessary compliance costs.<sup>127</sup> We do not expect these compliance costs to be significant since these registrants likely already possess the information required by the amendments. However, to the extent that such information is not readily accessible or needs to be formatted to comply with the required disclosure, registrants would incur additional costs.<sup>128</sup>

The required disclosures may impact the cost of capital for some affected registrants. As discussed above, empirical evidence suggests that the information elicited by the required disclosures is, in general, related to potential risks and more broadly to firm value.<sup>129</sup> We discuss the potential impact of the required disclosures on affected registrants' cost of capital further below, but note that the magnitude of any such impact is likely to be moderated depending on the extent information is otherwise available to investors.

The required disclosure regarding the use of a non-inspected firm to audit the registrant's annual report, which will now be required in a standardized manner, may lead investors to re-

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<sup>127</sup> See letter from China Petroleum.

<sup>128</sup> For the purpose of the Paperwork Reduction Act ("PRA"), 44 U.S.C. 3501 *et seq.*, we estimate that affected registrants will incur on average one burden hour to prepare and review the information needed for the HFCA Act Section 3 disclosure requirements. See *infra* Section V.C.

<sup>129</sup> See *supra* Section IV.A.

evaluate potential risks related to financial reporting quality due to the inability of the PCAOB to inspect the auditors of these registrants. Some academic literature finds that PCAOB oversight is broadly related to improvements of audit quality, and also investor perceptions of such audit quality.<sup>130</sup> As described above, many registrants already disclose the risks or decreased benefits associated with using a non-inspected auditor.<sup>131</sup> Given the extent to which information specifically required in the new disclosures overlaps with disclosures already observed in practice, in addition to the information being available from other sources such as the PCAOB, we expect the impact of these specific required disclosures on affected registrants' cost of capital to be small.

Section 3 of the HFCA Act also requires registrants to disclose information in a standardized manner in annual reports about their ownership and control structures, including the magnitude of direct equity ownership by a government in non-cooperating foreign jurisdictions and the degree of control a government in the non-cooperating jurisdiction may exert on the registrant through channels other than ownership. Providing standardized disclosure could facilitate more efficient comparisons of government ownership and control information across Commission-Identified Foreign Issuers and thus reduce investor search costs.

The amendments also will require registrants to disclose information about potential additional links to the CCP. Such disclosure is likely to be informative of the registrant's governance, and may also lead investors to re-assess potential political risks that may not have been previously known through existing registrants' disclosures. For example, such links between the registrant and the CCP may indicate increased political influence on registrants'

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<sup>130</sup> *See id.*

<sup>131</sup> *See supra* Section IV.B.1.

decision-making processes and consequent impacts on registrants' value. While some, but not all, of the information in the required disclosures may already be publicly available through disclosures in forms other than in annual reports, the content of such disclosures may not be standardized across registrants. We expect these specific disclosures may potentially impact registrants' cost of capital, particularly for registrants about which such information is not otherwise known by the market.

## **2. Benefits and Costs of HFCA Act Submission Requirement**

The amendments implementing the submission requirement of Section 104(i)(1)(B) of the Sarbanes-Oxley Act (as added by Section 2 of the HFCA Act) provide that a Commission-Identified Issuer that is not owned or controlled by a foreign governmental entity in a foreign jurisdiction that prevents PCAOB inspections must submit documentation to the Commission that establishes that the registrant is not so owned or controlled. As discussed above, the amendments specify that if an affected registrant is owned or controlled by a foreign governmental entity, it will not be required to submit such documentation. We estimate in the baseline that a large majority of current registrants that are potential future Commission-Identified Issuers are also foreign issuers that will be subject to the disclosures required by Section 3 of the HFCA Act. Therefore, we expect the submission requirement to serve as a complement to these required disclosures.

### **a. Investors**

We anticipate that requiring Commission-Identified Issuers to provide documentation to support a lack of foreign control will provide further reassurance to investors that the registrants' disclosures in this regard are materially accurate and complete. In particular, because the submission requirement generally would apply to those Commission-Identified Issuers who

otherwise do not disclose that they are owned or controlled by a foreign governmental entity, this requirement will provide some reassurance to investors that such control does not exist. We believe that greater certainty about which Commission-Identified Issuers lack governmental ownership and control may improve investors' assessments of the risks of investing in Commission-Identified Issuers' securities. One commenter suggested that registrants typically are not providing the detailed disclosures required by the HFCA Act and that current risk factor disclosure tends to be insufficient for investors to understand the consequences of non-inspection.<sup>132</sup> Since the submitted documentation will be publicly available, we expect the reassurance benefit to be larger than if the submission were available only to the Commission. Because affected registrants will have flexibility to determine the specific types of documentation to submit to the Commission, we expect the magnitude of the reassurance benefit to depend on the nature of information issuers submit. We generally expect this reassurance benefit to be limited given the HFCA Act's required Section 3 disclosure and other information about ownership and control required by existing Commission rules.<sup>133</sup>

Because we expect the submission requirement to impose (on average) only minor compliance costs on affected registrants and no other significant costs, we also do not generally expect any significant negative effects on investors from this requirement, such as a reduction in the prices of affected registrants' securities they currently own.

#### **b. Registrants**

Commission-Identified Issuers who lack ownership or control by a governmental entity in the foreign jurisdiction of the registered public accounting firm that the PCAOB is unable to

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<sup>132</sup> See letter from U.S. Acctg. Academics.

<sup>133</sup> See *supra* Section IV.B.1 for a description of current regulatory requirements regarding disclosure of ownership and control more generally.

inspect or investigate completely will incur some direct compliance costs related to producing the documentation they will be required to submit to the Commission. The magnitude of these compliance costs will depend on how easily the affected registrants can produce documentation to satisfy the submission requirement. The amendments do not specify particular types of documentation that can or must be submitted to satisfy this requirement. Affected registrants will thus have flexibility to determine how best to establish that they are not owned or controlled by a foreign governmental entity. This should help limit compliance costs, as registrants will be able to produce documentation that is suited to their particular circumstances. At the same time, at least as an initial matter, uncertainty about the scope of the requirement could lead some registrants to seek additional advice from attorneys and other advisers, which could marginally increase compliance costs. Overall, because we expect that affected registrants will have information readily available about their ownership structures and controlling parties, we expect the direct compliance costs associated with this requirement will be minor.<sup>134</sup>

### **3. Impact on Efficiency, Competition, and Capital Formation**

As discussed above, the required disclosures may provide new or more easily accessible information about whether registrants have retained non-inspected registered auditors and whether such registrants are owned or controlled by governmental entities of the foreign jurisdictions that prevent PCAOB inspections. To the extent this disclosed information is new or reduces search costs, we expect it could potentially reduce information asymmetries in securities markets, thereby improving price efficiency and helping investors achieve more efficient portfolio allocations. Overall, we believe that any efficiency gains will be modest since the potential increase in informational content and reduction in search costs to investors is likely to

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<sup>134</sup> See *supra* note 128.

be limited given existing disclosures.

To the extent the amendments will reduce information asymmetries, affected registrants may experience a change in cost of capital (either a reduction or an increase is possible, depending on circumstances), which may in turn affect capital formation. However, similar to any effects on efficiency, we expect such capital formation effects to be small in aggregate. Likewise, we do not expect the amendments to significantly impact overall competition, based on the expected low compliance costs for registrants and the expected limited incremental impact on investors' information environment. However, we do not rule out that there could be instances where the required disclosures provide new information about some registrants that could potentially impact (either positively or negatively) their individual competitive situation due to investors' reassessment of such registrants' risk and prospects.

## **V. Paperwork Reduction Act**

### **A. Background**

Certain provisions of Form 10-K and Form 20-F that will be affected by the amendments contain "collection of information" requirements within the meaning of the PRA.<sup>135</sup> The Commission is submitting the final amendments to the Office of Management and Budget ("OMB") for review in accordance with the PRA.<sup>136</sup> The titles for the collections of information

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<sup>135</sup> See *supra* note 128. As noted in the Economic Analysis section, see *supra* Section IV, based on recent Form 40-F filings, no Form 40-F registrants reported having retained a registered public accounting firm located in a foreign jurisdiction that we believe the PCAOB may determine it is unable to inspect or investigate completely because of a position taken by an authority in that foreign jurisdiction, and therefore we estimate that no Form 40-F registrants will be subject to the requirements of the final amendments upon their adoption. Accordingly, we are not making any revisions to the PRA burden estimates for Form 40-F at this time. Additionally, based on recent Form N-CEN filings, no registered investment company reported having retained a registered public accounting firm located in a foreign jurisdiction, and therefore we estimate that no registered investment companies will be subject to the requirements of the final amendments upon their adoption. Accordingly, we are not making any revisions to the PRA burden estimates for Form N-CSR at this time. See *supra* note 33.

<sup>136</sup> 44 U.S.C. 3507(d) and 5 CFR 1320.11.

are:

- “Form 10-K” (OMB Control No. 3235-0063); and
- “Form 20-F” (OMB Control No. 3235-0288).

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information requirement unless it displays a currently valid OMB control number. Compliance with the information collections is mandatory. Responses to the information collections are not kept confidential and there is no mandatory retention period for the information disclosed. The affected forms were adopted under the Exchange Act and set forth the disclosure requirements for annual reports filed by registrants to help investors make informed investment decisions. The hours and costs associated with preparing and filing the forms constitute reporting and cost burdens imposed by each collection of information.

#### **B. Summary of the Amendments**

As described in more detail above, we are adopting final amendments to implement the disclosure and submission requirements of the HFCA Act. The amendments will require certain disclosure from foreign issuers relating to foreign jurisdictions that prevent PCAOB inspections and require all applicable registrants to submit documentation to the Commission establishing that such a covered issuer is not owned or controlled by a governmental entity in that foreign jurisdiction.

#### **C. Burden and Cost Estimates Related to the Amendments**

We anticipate that new disclosure and submission requirements will increase the burdens and costs for these registrants. We derived our burden hour and cost estimates by estimating the average amount of time it would take a registrant to prepare and review the required disclosure and submission, as well as the average hourly rate for outside professionals who assist with such

preparation. In addition, our burden estimates are based on several assumptions. For the HFCA Act Section 3 disclosure requirements we estimated the number of affected registrants by determining the number of foreign issuer registrants that retained registered public accounting firms that issued an audit report and are located in a jurisdiction where obstacles to PCAOB inspections exist. For the Section 104(i)(1)(B) of the Sarbanes-Oxley Act (as added by Section 2 of the HFCA Act) submission requirements, we estimated the number of affected registrants by determining the number of registrants that retained registered public accounting firms that issued an audit report and are located in a jurisdiction where obstacles to PCAOB inspections exist. Based on these estimates, for purposes of the PRA, we estimate that there will be:

- No affected Form 10-K filers for the HFCA Act Section 3 disclosure requirements and 55 affected filers for the Section 104(i)(1)(B) of the Sarbanes-Oxley Act submission requirement; and
- Two hundred and twenty affected Form 20-F filers for the HFCA Act Section 3 disclosure requirements and 206 affected filers for the Section 104(i)(1)(B) of the Sarbanes-Oxley Act submission requirement.<sup>137</sup>

Commission-Identified Issuers will generally have information readily available about their audit arrangements, ownership structures, and controlling parties. Therefore, we estimate that the average incremental burden for an affected registrant to prepare the submission would be

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<sup>137</sup> *See supra* Section IV.B.2.a. Based on the data and analysis described in Section IV above, for purposes of the PRA we estimate that approximately 275 registrants may be affected by the rules, of which we estimate 20 percent are U.S. registrants that file on Form 10-K (55 registrants) and 80 percent are foreign issuers that file on Form 20-F (220 registrants). For purposes of the HFCA Act Section 3 disclosure requirement, we estimate that only foreign filers filing on Form 20-F will be required to provide the disclosure (220 registrants). For purposes of the Section 104(i)(1)(B) of the Sarbanes-Oxley Act submission requirement, we estimate that approximately five percent of the affected registrants are state-owned entities and will not be required to prepare the submission. As a result, we estimate that U.S. registrants that file on Form 10-K (55 registrants) and foreign issuers that file on Form 20-F but are not state-owned entities (206) will be required to provide the submission.

one hour and for an affected registrant that is a foreign issuer to prepare the disclosure would be one hour. These estimates represent the average burdens for all affected registrants, both large and small.<sup>138</sup> In deriving our estimates, we recognize that the burdens will likely vary among individual registrants based on a number of factors, including the size and complexity of their operations. We believe that some registrants will experience costs in excess of this average and some registrants may experience less than the average costs.

The table below shows the total annual compliance burden, in hours and in costs, of the collection of information resulting from the final amendments.<sup>139</sup> The burden estimates were calculated by multiplying the estimated number of responses by the estimated average amount of time it would take a registrant to prepare and review the required information. The portion of the burden carried by outside professionals is reflected as a cost, while the portion of the burden carried by the registrant internally is reflected in hours. For purposes of the PRA, we estimate that 75 percent of the burden of preparation of Form 10-K and Form 20-F is carried by the registrant internally and that 25 percent of the burden of preparation is carried by outside professionals retained by the registrant at an average cost of \$400 per hour.<sup>140</sup>

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<sup>138</sup> As discussed above in Section II.C., the final amendments also include structured data tagging requirements pertaining to the auditor name and jurisdiction on the audit report signed by the registered public accounting firm in the registrant's Form 10-K, Form 20-F, and Form 40-F. However, we believe that any associated burden resulting from this requirement will be encompassed within the overall PRA burden estimates for these forms because the final amendments add only a few discrete data points to an affected registrant's existing tagging obligations. Affected registrant are currently required to tag specified information in the relevant forms. *See generally* 17 CFR 232.405 (Rule 405 Regulation S-T) and 232.406 (Rule 406 of Regulation S-T), paragraphs 101 and 104 to "Instructions as to Exhibits" in Form 20-F, paragraphs 15 and 17 to General Instruction B in Form 40-F.

<sup>139</sup> The table's estimated number of responses aggregates the responses for both the disclosure requirement and the submission requirement. Some registrants will be counted twice, once for each response. For convenience, the estimated hour and cost burdens in the table have been rounded to the nearest whole number.

<sup>140</sup> We recognize that the costs of retaining outside professionals may vary depending on the nature of the professional services, but for purposes of this PRA analysis, we estimate that such costs will be an average of \$400 per hour. This estimate is based on consultations with several registrants, law firms and other persons who regularly assist registrants in preparing and filing periodic reports with the Commission.

**Table 1. Incremental Paperwork Burden under the Final Amendments.**

	Estimated number of affected responses (A)	Incremental Burden Hours/Form (B)	Total Incremental Burden Hours (C)=(A)*(B)	75% Company (D)=(C)*0.75	25% Professional (E)=(C)*0.25	Professional Costs (F)=(E)*\$400
Form 10-K (submission)	55	1	55	41	14	\$5,600
Form 20-F (submission)	206	1	206	155	52	\$20,800
Form 20-F (disclosure)	220	1	220	165	55	\$22,000

## **VI. Statutory Authority**

The amendments contained in this release are being adopted under the authority set forth in Sections 2 and 3 of the HFCA Act, Section 104 of the Sarbanes-Oxley Act, Sections 3, 12, 13, 15(d), and 23(a) of the Exchange Act, and Sections 8(b), 24(a), 30(a), and 38(a) of the Investment Company Act.

### **List of Subjects in 17 CFR Parts 200, 232, and 249**

Reporting and recordkeeping requirements, Securities.

## **TEXT OF RULE AMENDMENTS**

In accordance with the foregoing, the Commission amends title 17, chapter II of the Code of Federal Regulations as follows:

### **PART 200—ORGANIZATION; CONDUCT AND ETHICS; AND INFORMATION AND REQUESTS**

#### **Subpart A—Organization and Program Management**

1. The authority citation for part 200, subpart A, continues to read, in part, as follows:

Authority: 15 U.S.C. 77c, 77o, 77s, 77z-3, 77sss, 78d, 78d-1, 78d-2, 78o-4, 78w, 78ll(d), 78mm, 80a-37, 80b-11, 7202, and 7211 *et seq.*, unless otherwise noted.

\* \* \* \* \*

Section 200.30-1 is also issued under 15 U.S.C. 77f, 77g, 77h, 77j, 78c(b) 78l, 78m, 78n, 78o(d).

\* \* \* \* \*

2. Amend § 200.30-1 by adding to paragraph (m) to read as follows:

**§ 200.30-1 Delegation of authority to Director of Division of Corporation Finance.**

\* \* \* \* \*

(m) With respect to Section 104(i)(2)(A) of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7214 (as amended by Pub. L. 116-222)), to identify each “covered issuer,” as that term is defined in Section 104(i)(1)(A) of the Sarbanes-Oxley Act of 2002, that has retained a registered public accounting firm to issue an audit report where that registered public accounting firm has a branch or office that is located in a foreign jurisdiction and Public Company Accounting Oversight Board has determined that it is unable to inspect or investigate completely because of a position taken by an authority in the foreign jurisdiction.

**PART 232—REGULATION S-T—GENERAL RULES AND REGULATIONS FOR ELECTRONIC FILINGS**

3. The general authority citation for part 232 continues to read as follows:

Authority: 15 U.S.C. 77c, 77f, 77g, 77h, 77j, 77s(a), 77z-3, 77sss(a), 78c(b), 78l, 78m, 78n, 78o(d), 78w(a), 78ll, 80a-6(c), 80a-8, 80a-29, 80a-30, 80a-37, 7201 *et seq.*; and 18 U.S.C. 1350, unless otherwise noted.

\* \* \* \* \*

4. Effective January 10, 2022, through July 1, 2023, amend §232.405 by adding paragraph (c)(1)(iii)(C) to read as follows:

**§ 232.405 Interactive Data File submissions.**

\* \* \* \* \*

(c) \* \* \*

(1) \* \* \*

(iii) \* \* \*

(C) *Additional elements.* Annual reports on forms 10-K, 20-F or 40-F filed for periods after December 15, 2021, must contain all applicable data elements from the most recently updated relevant standard taxonomy; and

\* \* \* \* \*

**PART 249 — FORMS, SECURITIES EXCHANGE ACT OF 1934**

5. The general authority citation for part 249 and sectional authority citations for §§249.220f, 249.240f, 249.310, and 249.331 continue to read as follows:

Authority: 15 U.S.C. 78a *et seq.* and 7201 *et seq.*; 12 U.S.C. 5461 *et seq.*; 18 U.S.C. 1350; Sec. 953(b) Pub. L. 111-203, 124 Stat. 1904; Sec. 102(a)(3) Pub. L. 112-106, 126 Stat. 309 (2012), Sec. 107 Pub. L. 112-106, 126 Stat. 313 (2012), Sec. 72001 Pub. L. 114-94, 129 Stat. 1312 (2015), and secs. 2 and 3 Pub. L. 116-222, 134 Stat. 1063 (2020), unless otherwise noted.

Section 249.220f is also issued under secs. 3(a), 202, 208, 302, 306(a), 401(a), 401(b), 406 and 407, Pub. L. 107-204, 116 Stat. 745, and secs. 2 and 3, Pub. L. 116-222, 134 Stat. 1063.

Section 249.240f is also issued under secs. 3(a), 202, 208, 302, 306(a), 401(a), 406 and 407, Pub. L. 107-204, 116 Stat. 745.

\* \* \* \* \*

Section 249.310 is also issued under secs. 3(a), 202, 208, 302, 406 and 407, Pub. L. 107-204, 116 Stat. 745.

\* \* \* \* \*

Section 249.331 is also issued under 15 U.S.C. 78j-1, 7202, 7233, 7241, 7264, 7265; and 18 U.S.C. 1350.

\* \* \* \* \*

6. Amend Form 20-F (referenced in § 249.220f) by revising Item 16I.(b) to read as follows:

**Note: The text of Form 20-F does not, and this amendment will not, appear in the Code of Federal Regulations.**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 20-F**

\* \* \* \* \*

**PART II**

\* \* \* \* \*

**Item 16I. Disclosure Regarding Foreign Jurisdictions that Prevent Inspections.**

\* \* \* \* \*

(b) A registrant that is a foreign issuer, as defined in 17 CFR 240.3b-4, identified by the Commission pursuant to Section 104(i)(2)(A) of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7214(i)(2)(A)) as having retained, for the preparation of the audit report on its financial statements included in the Form 20-F, a registered public accounting firm that has a branch or office that is located in a foreign jurisdiction and that the Public Company Accounting Oversight

Board has determined it is unable to inspect or investigate completely because of a position taken by an authority in the foreign jurisdiction, for each year in which the registrant is so identified, must provide the below disclosures. Also, any such identified foreign issuer that uses a variable-interest entity or any similar structure that results in additional foreign entities being consolidated in the financial statements of the registrant is required to provide the below disclosures for itself and its consolidated foreign operating entity or entities. A registrant must disclose:

\* \* \* \* \*

7. Amend Form 40-F (referenced in § 249.240f) by revising paragraph B.18(b) to read as follows:

**Note: The text of Form 40-F does not, and this amendment will not, appear in the Code of Federal Regulations.**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 40-F**

\* \* \* \* \*

**GENERAL INSTRUCTIONS**

\* \* \* \* \*

**B. Information to be Filed on this Form**

(18) Disclosure Regarding Foreign Jurisdictions that Prevent Inspections.

\* \* \* \* \*

(b) A registrant that is a foreign issuer, as defined in 17 CFR 240.3b-4, identified by the Commission pursuant to Section 104(i)(2)(A) of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7214(i)(2)(A)) as having retained, for the preparation of the audit report on its financial

statements included in the Form 40-F, a registered public accounting firm that has a branch or office that is located in a foreign jurisdiction and that the Public Company Accounting Oversight Board has determined it is unable to inspect or investigate completely because of a position taken by an authority in the foreign jurisdiction, for each year in which the registrant is so identified, must provide the below disclosures. Also, any such identified foreign issuer that uses a variable-interest entity or any similar structure that results in additional foreign entities being consolidated in the financial statements of the registrant is required to provide the below disclosures for itself and its consolidated foreign operating entity or entities. A registrant must disclose:

\* \* \* \* \*

8. Amend Form 10-K (referenced in §249.310) by revising Item 9C(b) to Part II to read as follows:

**Note: The text of Form 10-K does not, and this amendment will not, appear in the Code of Federal Regulations.**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-K**

\* \* \* \* \*

**Part II**

\* \* \* \* \*

**Item 9C. Disclosure Regarding Foreign Jurisdictions that Prevent Inspections.**

(b) A registrant that is a foreign issuer, as defined in 17 CFR 240.3b-4, identified by the Commission pursuant to Section 104(i)(2)(A) of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7214(i)(2)(A)) as having retained, for the preparation of the audit report on its financial

statements included in the Form 10-K, a registered public accounting firm that has a branch or office that is located in a foreign jurisdiction and that the Public Company Accounting Oversight Board has determined it is unable to inspect or investigate completely because of a position taken by an authority in the foreign jurisdiction, for each year in which the registrant is so identified, must provide the below disclosures. Also, any such identified foreign issuer that uses a variable-interest entity or any similar structure that results in additional foreign entities being consolidated in the financial statements of the registrant is required to provide the below disclosures for itself and its consolidated foreign operating entity or entities. A registrant must disclose:

\* \* \* \* \*

9. Amend Form N-CSR (referenced in §§249.331 and 274.128) by revising paragraph (j) to Item 4 to read as follows:

**Note: The text of Form N-CSR does not, and this amendment will not, appear in the Code of Federal Regulations.**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM N-CSR**

\* \* \* \* \*

Item 4. Principal Accountant Fees and Services

\* \* \* \* \*

(j) A registrant that is a foreign issuer, as defined in 17 CFR 240.3b-4, identified by the Commission pursuant to Section 104(i)(2)(A) of the Sarbanes-Oxley Act of 2002 (15 U.S.C. 7214(i)(2)(A)), as having retained, for the preparation of the audit report on its financial statements included in the Form N-CSR, a registered public accounting firm that has a branch or office that is located in a foreign jurisdiction and that the Public Company Accounting Oversight

Board has determined it is unable to inspect or investigate completely because of a position taken by an authority in the foreign jurisdiction, for each year in which the registrant is so identified, must provide the below disclosures. Also, any such identified foreign issuer that uses a variable-interest entity or any similar structure that results in additional foreign entities being consolidated in the financial statements of the registrant is required to provide the below disclosures for itself and its consolidated foreign operating entity or entities. A registrant must disclose:

\* \* \* \* \*

By the Commission.

Dated: December 2, 2021.

Vanessa A. Countryman,

Secretary.