

SEC Reporting & Compliance Alert

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One Manhattan West
New York, NY 10001
212.735.3000

SEC Adopts Final Amendments Implementing Mandates of the Holding Foreign Companies Accountable Act

On December 2, 2021, the U.S. Securities and Exchange Commission (SEC) adopted final amendments implementing the disclosure and submission requirements of the Holding Foreign Companies Accountable Act (HFCA Act). In addition, the adopting release establishes the SEC's procedures for (i) determining whether a registrant is a "Commission-Identified Issuer" under the HFCA Act and (ii) prohibiting the trading of a Commission-Identified Issuer's securities.

The final amendments will go into effect 30 days after publication in the Federal Register. The earliest that the SEC could identify a Commission-Identified Issuer would be after companies file their annual reports for 2021 (*i.e.*, spring 2022 for calendar-year issuers). **The earliest any trading prohibitions would apply would be in 2024, once an issuer has been a Commission-Identified Issuer for three consecutive years (2022, 2023 and 2024).**

Background

Registrants with securities listed on a U.S. securities exchange must comply with the registration and reporting provisions of the Securities Exchange Act of 1934, as amended (Exchange Act). These requirements include annually filing audited financial statements with the SEC. The auditor of those financial statements — whether a U.S. auditor or a non-U.S. auditor — must be registered with, and therefore subject to inspection by, the Public Company Accounting Oversight Board (PCAOB).

The HFCA Act, which became effective on January 1, 2021, directs the SEC to prohibit securities of a registrant from being listed on any U.S. securities exchanges if, for three consecutive years, the PCAOB determines it was unable to inspect the auditor of the registrant's financial statements.¹ In addition, the HFCA Act also requires a foreign registrant to provide certain disclosures if the registrant files an annual report that includes an audit report from an auditor that was not subject to PCAOB inspection.

¹ See our November 8, 2021, client alert "[SEC Approves PCAOB Rule Establishing Framework for Determinations Under the Holding Foreign Companies Accountable Act](#)" for additional information about the PCAOB's determination process.

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Summary of SEC Implementation Amendments

Commission-Identified Issuer Determination

A “Commission-Identified Issuer” is an issuer identified by the SEC as having filed an annual report containing an audit report issued by a registered public accounting firm that the PCAOB has determined it is unable to inspect or investigate completely because of a position taken by an authority in the foreign jurisdiction (PCAOB-Identified Firm).² The SEC will identify such issuers promptly after the filing of their annual report by evaluating (via Inline XBRL tagging or other structured data) whether the issuer’s annual report contains an audit report signed by a PCAOB-Identified Firm.

The SEC will then “provisionally identify” the issuer as a Commission-Identified Issuer on the SEC’s website at www.sec.gov/HFCAA. Provisionally identified issuers will have 15 business days to email the SEC to dispute the identification, after which the determination becomes conclusive.

Trading Prohibition

The SEC will impose an initial trading prohibition on a registrant as soon as practicable after it is conclusively identified as a Commission-Identified Issuer for three consecutive years. The prohibition will apply to trading on a national securities exchange and in the over-the-counter market. If the SEC ends the initial trading prohibition and, thereafter, the registrant is again determined to be a Commission-Identified Issuer, the SEC will impose a subsequent trading prohibition on the registrant for a minimum of five years. In both instances, the SEC’s order will be effective on the fourth business day after it is published.

To end an initial or subsequent trading prohibition, a Commission-Identified Issuer must certify that it has retained or will retain a non-PCAOB-Identified Firm. To make that certification, the Commission-Identified Issuer must file financial statements that include an audit report signed by a non-PCAOB-Identified Firm.

Submission Requirements

A Commission-Identified Issuer that is **not** owned or controlled by a governmental entity in the foreign jurisdiction of its PCAOB-Identified Firm must submit to the SEC documentation establishing that the registrant is not so owned or controlled. The

documentation must be submitted through EDGAR on or before the due date of the issuer’s annual report. It can be submitted either with the annual report, on Form 8-K or 6-K, as applicable, or using another appropriate method.

Although the term “owned or controlled” is not defined in the HFCA Act, the SEC believes the term has the same meaning as the term “control” under the Exchange Act and Exchange Act rules.³ Moreover, the SEC declined to provide a list of what documentation may demonstrate that the Commission-Identified Issuer is not owned or controlled by the relevant governmental entity. Instead, Commission-Identified Issuers will have flexibility to determine the appropriate documentation to submit in response to the requirement.

A Commission-Identified Issuer that **is** owned or controlled by a foreign governmental entity is not required to submit such documentation.

Disclosure Requirements

A Commission-Identified Issuer that is also a foreign issuer (Identified Foreign Issuer) will be required to disclose in its annual report:

- the PCAOB-Identified Firm that caused the issuer to be identified as a Commission-Identified Issuer during the period covered by the form;
- the percentage of the registrant’s shares owned by governmental entities in the foreign jurisdiction in which the issuer is incorporated or otherwise organized;
- whether governmental entities in the foreign jurisdiction where that registered public accounting firm is located have a controlling financial interest in 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.

² If a public company’s annual report 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” will be deemed retained for purposes of the final rule.

³ Under Rule 405, “control” is defined as “the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise.” However, control status is dependent in large part on the facts and circumstances. For example, a person or entity that owns a small percentage of shares or that is represented on the board of directors may have “control” if they have the ability directly or indirectly to affect a company’s management or policies.

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In addition to providing the required disclosures for the Commission-Identified Foreign Issuer, the issuer must look through a variable-interest entity (VIE) or any structure that results in additional foreign entities being consolidated in its financial statements and provide the required disclosures about any consolidated operating company or companies in the relevant jurisdiction.

A registrant will be required to provide this disclosure for each year in which it is an Identified Foreign Issuer. For example, 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.

Contacts

Brian V. Breheny

Partner / Washington, D.C.
202.371.7180
brian.breheny@skadden.com

Raquel Fox

Partner / Washington, D.C.
202.371.7050
raquel.fox@skadden.com

Z. Julie Gao

Partner / Hong Kong
852.3740.4863
julie.gao@skadden.com

Kenneth W. Chase

Counsel / Hong Kong
852.3740.4755
kenneth.chase@skadden.com

Leo W. Chomiak

Associate / Washington, D.C.
202.371.7511
leon.chomiak@skadden.com

Law clerk **Dennis Stinchcomb** contributed to this article.