

Holding Foreign Companies Accountable Act Signed into Law

December 30, 2020

The Holding Foreign Companies Accountable Act (Act), which was signed into law by President Trump on December 18, 2020, amends the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley) and requires the Securities and Exchange Commission (SEC) to *identify* reporting public companies using registered public accounting firms located in a foreign country that prevents the Public Company Accounting Oversight Board (PCAOB) from auditing the accounting firm and to *prohibit* trading of securities of such public companies in U.S. markets after three consecutive non-inspection years. The Act also *imposes* additional public disclosure obligations on foreign issuers subject to the Act.

More specifically, the Act imposes the following requirements on the SEC and covered issuers:

- The SEC must identify each issuer required to file reports under Section 13 or 15(d) of the Securities Exchange Act of 1934 (covered issuer) that retains a registered public accounting firm to prepare an audit report on the issuer's financial statements contained in any such publicly filed reports, where that accounting firm is located in a foreign jurisdiction that prevents that PCAOB from investigating or inspecting the accounting firm.
- Identified covered issuers must then submit documentation to the SEC establishing that the issuer is not owned or controlled by a foreign governmental entity of such foreign jurisdiction. The SEC is required to issue rules to establish the manner and form for implementing these submissions within 90 days after the enactment of the Act.
- If the SEC determines that a covered issuer has had *three consecutive* "non-inspection years," the SEC is required to prohibit trading of securities of the covered issuer on any national securities exchange or other method regulated by the SEC, including "over the counter" trading. A non-inspection year is defined as a year beginning *after the enactment date of the Act* during which the covered issuer is so identified by the SEC with respect to every report filed by the covered issuer during the year. The trading prohibition will be removed by the SEC once the covered issuer certifies that it has retained a registered public accounting firm inspected by the PCAOB to the satisfaction of the SEC. However, if the SEC subsequently determines that the issuer has another non-inspection year, the SEC must again prohibit trading *but this time for five years* after the prohibition is imposed. The trading prohibition will be removed after the end of the five-year period if the covered issuer certifies to the SEC that it has retained a PCAOB inspected registered public accounting firm.
- Foreign issuers (foreign governments, foreign nationals or corporations or other organizations organized under the laws of a foreign country) that are covered issuers under the Act are required to make the following additional disclosures in their annual reports on Form 10-K or Form 20-F filed with respect to each non-inspection year: the PCAOB was not able to inspect or investigate the auditing registered public accounting firm; the percentage ownership of the issuer by governmental entities in the foreign jurisdiction in which the issuer is incorporated or otherwise organized; whether governmental entities in the applicable foreign jurisdiction preventing PCAOB audit of its registered public accounting firm have a controlling financial interest with respect to the issuer; the name of each official of the Chinese Communist Party on 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 Chinese Communist Party and text of any such charter.

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According to a statement issued on December 18, 2020, the day the Act was signed by President Trump, SEC Chairman Jay Clayton has directed the SEC staff, in view of the "substantial overlap" of the Act and recommendations made by the President's Working Group on Financial Markets in its July 2020 Report on Protecting United States Investors from Significant Risks from Chinese Companies (PWG Report), "to consider providing a single consolidated proposal for the Commission's consideration on issues related to the PCAOB's access to audit work papers, exchange listing standards, and trading prohibitions." The SEC Chairman has also asked the staff "to consider additional issues relating to the Act's implementation, including how the Act's disclosure requirements can be implemented expeditiously and how any actual or perceived uncertainty can be addressed in a manner consistent with congressional intent as well as investor protection and the fair and orderly operation of our markets."

This Act is one of a series of measures passed by the Trump administration focusing on financial investment links between U.S. and China. Last month, President Trump issued an executive order prohibiting American investment in Chinese military companies. For details, see our previous alert available at <https://www.millercanfield.com/resources-Trump-Bans-American-Investment-Chinese-Military-Companies.html>. And last week, the U.S. Department of Commerce Bureau of Industry and Security (BIS) issued the Military End User List providing a "first tranche" of over 100 designated military end users from China and Russia for restricting exports to the two countries. For details, see our previous alert available at <https://www.millercanfield.com/resources-Military-End-User-List-Exports-China-Russia.html>.

The Act is available at <https://www.congress.gov/116/bills/s945/BILLS-116s945enr.pdf>. If you have any questions about the Act, please contact the authors or your Miller Canfield attorney.