

The Competition of Systems in the Market for Listings

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A. Introduction

Before the ink was dry on the Sarbanes-Oxley Act of 2002, American academics and policy-makers were assessing the effects of the new legislation on the competitiveness of the U.S. markets. In one camp are those who argue that the law is a short-sighted response to a short-lived crisis, driving non-U.S. issuers from the U.S. markets and hampering the competitiveness of the markets. In the other camp are those who maintain that the legislation was long overdue and will enhance competitiveness by attracting to the United States firms that are eager to demonstrate their ability to comply with robust regulatory norms. This paper discusses the debate and presents preliminary empirical data from four countries bearing on why a non-U.S. company that decided to register and sell shares in the United States would deregister and exit the U.S. markets. The initial results suggest strongly that deregistering firms are leaving not necessarily because of regulatory costs, but due to lackluster performance compared to their peers. This conclusion should be important to policy-makers and warrants further study.

Sarbanes-Oxley was a watershed. Ever since the enactment of the federal securities laws in the 1930s, the U.S. Congress and the Securities and Exchange Commission (“SEC”) steered clear of regulating the governance of corporations

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registered with the SEC and listed on the major exchanges. Although exceptions exist, disclosure, not regulation, has been the essential ingredient of the U.S. federal securities laws.¹ Governance of most companies was left primarily to state legislatures and state courts.

Sarbanes-Oxley changed the landscape. The Sarbanes-Oxley Act was a reaction to the corporate debacles of 2001 and 2002 and Congress designed the law to correct systemic weaknesses in corporate governance. For the first time, Congress reached into the structure of public companies to require officers, directors, and others to pay attention to matters previously left to the province of state regulation. The statute required top officers to certify the integrity of the company's financial statements,² prohibited a company from making certain loans to its officers and directors,³ required management to report on the company's internal controls,⁴ enhanced the independence of the company's audit committee,⁵ and directed the SEC to adopt rules requiring companies to implement a code of ethics.⁶ The Act also established new standards for auditor independence and created the Public Company Accounting Oversight Board ("PCAOB")

¹ J Seligman, *The Transformation of Wall Street* (3rd edn Aspen New York 2003) 38.

² Sarbanes-Oxley Act of 2002 s 302, 15 USC s 7241 (2006).

³ Ibid s 402, 15 USC s 78m.

⁴ Ibid s 404, 15 USC s 7262.

⁵ Ibid ss 201a, 202-04, 15 USC s 78j-1.

⁶ Ibid s 406, 15 USC s 7264.

to regulate, oversee, inspect, and discipline audit firms.⁷ It even required new rules to regulate the conduct of lawyers practicing before the SEC.⁸ And this is only a partial list.

Shortly after its passage, commentators began calling the new legislation the most significant change to U.S. corporate governance since the Great Depression. Although the U.S. federal securities laws have been amended over the years, the changes wrought by Sarbanes-Oxley were seen as the most significant since the original laws were drafted.⁹ It was not long, therefore, before the plangent cries of the critics began.

Opponents of the new law echoed opponents of the newly born Securities Act of 1933 seventy years earlier. Those objecting to the 1933 Act argued in August of that year that the new law would hamper the competitiveness of the U.S. markets by forcing corporations to go offshore for capital.¹⁰ Similarly, critics of Sarbanes-Oxley maintained that the Act would cause companies considering initial public offerings (“IPOs”) in the United States to opt for London or Hong Kong instead. They also stated that Sarbanes-Oxley would encourage non-U.S. companies already cross-listed in the United States to delist and deregister to avoid new costs imposed by the statute.¹¹ Thus began an active

⁷ Ibid s 101, 15 USC s 7211.

⁸ Ibid s 307, 15 USC s 7245.

⁹ See H Grubel, ‘Regulators vs. Adam Smith’ *Wall Street Journal* (New York 3 October 2002) A14.

¹⁰ *Seligman* (n 1) 77.

¹¹ Joyce E Cutler, ‘PCAOB Member Disputes Reports Sarbanes-Oxley Has Hurt U.S. Markets’ (2007) 39 *Securities Regulation & Law Report* 926; R Clow, ‘Groups may delist to avoid tougher SEC rules’ *Financial Times* (London 24 October 2002) 2002 WLNR 6767325; John C Coffee, Jr, ‘Law and the Market: The Impact of Enforcement’ (2007) 156 *University of Pennsylvania Law Review* 229; Steven M Davidoff, ‘Regulating Listings in a Global Market’ (2007) 86 *North Carolina Law Review* 89; Larry E Ribstein, ‘Cross-listing and Regulatory Competition’ (2005) 1 *Review of Law & Economics* 97, 127.

debate in the popular and academic press on the topic of overregulation and whether the Congress and the SEC had gone too far, threatening the viability and competitiveness of the U.S. markets.

Several years have now passed since the enactment of Sarbanes-Oxley. After an initial flurry of SEC rulemaking to meet the deadlines imposed by Congress, the SEC has had an opportunity review whether it might ease the implementation of certain provisions of the Act, such as section 404, which requires reporting on internal controls. Over the past two years, in response to charges that U.S. regulators overreacted to the corporate failures of 2001 and 2002, the SEC has issued a number of deregulatory measures to reduce the costs of complying with the legislation.¹² In June 2007, for example, the SEC adopted an interpretive release to provide guidance regarding management's evaluation and assessment of internal controls over financial reporting, which permitted a risk-based evaluation of internal controls.¹³ In July 2007, the SEC approved PCAOB proposed Audit Standard No. 5 to eliminate what the SEC called the "unduly expensive and inefficient" requirements of Auditing Standard No. 2.¹⁴

¹² S Labaton, 'S.E.C. Eases Regulations on Business' *The New York Times* (New York 14 December 2006).

¹³ A Commission Guidance Regarding Management's Report on Internal Control Over Financial Reporting Under Section 13(a) or 15(d) of the Securities Exchange Act of 1934, Securities Act Release No 8,810, Exchange Act Release No 55,929, 72 Fed Reg 35,323 (27 June 2007).

¹⁴ See Press Release, Securities and Exchange Commission, 'SEC Approves PCAOB Auditing Standard No. 5 Regarding Audits of Internal Control Over Financial Reporting; Adopts Definition of "Significant Deficiency"' (25 July 2007) <<http://www.sec.gov/news/press/2007/2007-144.htm>> accessed 30 March 2008; see also Public Company Accounting Oversight Board, Order Approving Proposed Auditing Standard No. 5, An Audit of Internal Control Over Financial Reporting that is Integrated with an Audit of Financial Statements, a Related Independence Rule, and Conforming Amendments, Exchange Act Release

In addition, after initial speculation about how the Act might affect competitiveness, academic researchers have concluded a number of empirical studies shedding light on the actual effects of the new law. Although researchers continue to disagree, the disagreement and debate is becoming more informed than in the period shortly after Sarbanes-Oxley was passed. This paper adds to the growing literature on market competitiveness, presenting new data to help analyze whether overregulation is compromising competitiveness. We are particularly interested in non-U.S. companies that registered with the SEC before Sarbanes-Oxley and then decided to deregister from the SEC after passage of the Act. Why do the benefits of SEC registration no longer justify the costs?

To begin to answer that question, we examine the financial profiles of the deregistering firms compared to the stay-registered firms. Our preliminary results indicate that deregistering companies were poor performing companies compared to those companies that remained registered. This was the case in each of the four countries that were part of our initial survey: Great Britain, France, Germany, and Italy. The results differed for each country, but the overall trend was similar.

These results are consistent with several explanations, and the policy implications differ depending on the explanation. These results, for example, could suggest that regulatory requirements are not the impetus for firms to deregister. Rather firms deregister when, due to poor performance, they no longer attract investment from the host country. The results, however, also could suggest that additional regulatory requirements

No 56,142, 2007 WL 2577384 (27 July 2007) <<http://www.sec.gov/rules/pcaob/2007/34-56152.pdf>> accessed 30 March 2008.

cause companies to deregister and the added costs have greater negative effects on poor performing companies than on more profitable firms. Perhaps the additional regulatory costs imposed by Sarbanes-Oxley were significant enough to push poor performing companies over the brink and cause them to deregister. In this paper, we present the initial results of our study but forbear from making policy recommendations.

This paper proceeds as follows: Part B provides background with respect to non-U.S. firms that register with the SEC and cross-list on a U.S. exchange. Part C discusses reasons foreign companies would choose to cross-list. Part D addresses the extraterritorial application of the Sarbanes-Oxley legislation. Part E discusses the effects of the new law on market competitiveness. Part F is a brief literature review. Part G provides the methodology of our own empirical research and preliminary results. Part H concludes.

B. SEC Registration and Cross-Listing

Non-U.S. companies that access the U.S. markets are called foreign private issuers (“FPIs”) by the SEC – as distinguished from governmental issuers – and we adopt that convention in the remainder of this paper. Most FPIs access the U.S. markets by selling American Depositary Receipts (“ADRs”) to U.S. investors. ADRs are instruments created by depository banks. They are negotiable U.S. securities that represent a claim on the FPI’s publicly traded equity.¹⁵ Most investors prefer ADRs to

¹⁵ Termination of a Foreign Private Issuer’s Registration of a Class of Securities Under Section 12(g) and Duty to File Reports Under Section 13(a) or 15(d) of the Securities Exchange Act of 1934, Exchange Act Release No 55,540, International Series Release No 1,301, 72 Fed Reg 16,934, 16,935 n 21 (5 April 2007).

buying shares directly to mitigate the risk of currency fluctuations and the opacity of certain foreign regulations.¹⁶

FPIs can sell ADRs in the United States on four levels. Level 1 ADRs are sold over-the-counter without a listing on an exchange, and Level 1 ADRs are subject to an issuer exemption from registration and minimal regulation.¹⁷ Level 2 ADRs are registered under section 12 of the Securities Exchange Act of 1934. They are generally listed on an exchange and a company selling Level 2 ADRs must comply with most registration and reporting requirements of the relevant exchange and the SEC. Level 3 ADRs, like Level 2, are listed and traded on a U.S. exchange, and the selling company is subject to exchange and SEC rules. FPIs typically sell Level 3 ADRs when making a public offering in the United States and, as a result, Level 3 ADRs are subject to the Securities Act of 1933 as well as the registration and reporting requirements of the Exchange Act. Finally, Level 4 ADRs are for securities with limited trading and they are not subject to significant regulation. Sarbanes-Oxley applies to Level 2 and Level 3 ADRs.¹⁸

¹⁶ L Little 'ADR Trades Jumped to a Record in 2006' *Wall Street Journal* (New York 16 January 2007) C3.

¹⁷ See 17 CFR s 240.12g3-2(b) (2007).

¹⁸ See Kate Litvak, 'Sarbanes-Oxley and the Cross-Listing Premium' (2007) 105 *Michigan Law Review* 1857, 1865; Geoffrey Peter Smith, 'A Look at the Impact of Sarbanes-Oxley on Cross-Listed Firms' 5 (2007) <<http://ssrn.com/abstract=931051>> accessed 30 March 2008; *Ribstein* (n 11) 105.

¹⁹ Additional Form F-6 Eligibility Requirement Related to the Listed Status of Deposited Securities Underlying American Depositary Receipts, Securities Act Release No 8,287, Exchange Act Release No 48,482, International Series Release No 1,273, 81 SEC Docket 28 (11 September 2003).

The four levels of ADR trading give FPIs significant choice in accessing the U.S. markets. They also allow a FPI to change from one level to another, thereby lowering the regulatory burdens that might apply while, at the same time, maintaining some presence in the U.S. markets. Recently, when several FPIs have announced plans to deregister, they did not exit the U.S. markets completely. Instead, they converted their ADRs from Level 2 or Level 3 to Level 1 and the ADRs will continue to trade over-the-counter. SEC registration requirements, however, will no longer be applicable. Examples include U.K. companies, Imperial Chemical Industries, PLC and Spirent Communications, PLC.

A few foreign firms sell company shares – known as Global Shares – directly to U.S. investors. Global Shares trade in the United States the same way they trade in the firm’s home country – the same security is traded in two markets. According to the SEC, Global Shares can have some advantages over ADRs because a FPI selling Global Shares in the United States does not depend on a depository bank for services. Investors can be better served because Global Shares purchased outside the United States do not have to be converted to ADRs before sold on a U.S. exchange.¹⁹

C. Reasons to Cross-List

Non-U.S. companies presumably register with the SEC and list their shares in the United States because they believe the benefits of doing so outweigh the costs. In some cases, benefits are readily quantifiable, such as a cross-listing premium in valuation. In other cases, benefits are less quantifiable, or only quantifiable in the long term, such as

¹⁹ Additional Form F-6 Eligibility Requirement Related to the Listed Status of Deposited Securities Underlying American Depositary Receipts, Securities Act Release No 8,287, Exchange Act Release No 48,482, International Series Release No 1,273, 81 SEC Docket 28 (11 September 2003).

enhanced profile or visibility in the host country. Researchers have put forth several rationales for cross-listing, which generally fall under either a liquidity thesis or a bonding thesis.²⁰

According to the liquidity thesis, firms list on a foreign exchange for greater liquidity for their shares and easier access to capital. In the case of the United States, a cross-listing could enhance liquidity because U.S. markets are often considered deeper and more liquid than a company's home market. Cross-listing also might provide liquidity because U.S. investors face transaction costs when investing in foreign securities. A U.S. broker-dealer, for example, might be required to use a correspondent foreign broker-dealer to purchase non-U.S. shares. A U.S. investor also might face costs resulting from currency, regulatory, and clearing and settlement risks. These costs would be ameliorated if shares were offered in the United States and, therefore, a U.S. listing could result in increased demand.²¹

According to the bonding thesis, managers bond themselves by subjecting the company and themselves to tougher regulations, including robust disclosure, private liability, and governmental enforcement.²² Just like a company can play a role in deciding which laws will apply to it by deciding where to incorporate and establish a place of business, so too can a company decide which regulatory system will govern its

²⁰ See *Litvak* (n 18) 1861; *Coffee* (n 11) 284; Craig Doidge et al, 'Why Are Foreign Firms Listed in the U.S. Worth More?' (2004) 71 *Journal of Financial Economics* 205, 207-10; *Ribstein* (n 11) 104.

²¹ *Doidge et al* (n 20) 208.

²² *Coffee* (n 11) 285; John C Coffee, Jr, 'The Future as History: The Prospects for Global Convergence in Corporate Governance and Its Implications' (1999) 93 *Northwestern University Law Review* 641, 691-92; *Doidge et al* (n 20) 208-09.

capital-raising and share trading. By choosing to cross-list in a foreign market, a company can *opt in* to a particular regulatory regime that might be more onerous than that of its home country (even if the firm cannot *opt out* of regulations at home).²³

The bonding thesis assumes investors in a foreign firm may discount the share price to compensate for the risk that self-dealing or other value-impairing activity will occur. According to the bonding thesis, a cross-listing is meant to convince investors that the firm has decided to forgo private benefits of self-dealing in exchange for reducing the discount investors might otherwise apply. This is known as bonding because the managers' *bond* is the risk of monetary penalties or other sanctions that might be imposed in the event of non-compliance with the more stringent rules of the host country.²⁴ After reviewing relevant data, Larry Ribstein recently concluded that bonding is the primary explanation for cross-listing.²⁵

Liquidity and bonding hypotheses are not mutually exclusive, and they are consistent with other evidence suggesting that a third reason to cross-list is to signal to investors that the firm wishes to conduct a successful public offering of debt or equity.²⁶ By cross-listing, the firm signals its high quality and strong future prospects.²⁷ Several academic studies have borne out the bonding and signaling hypotheses. Cross-listing

²³ See *Ribstein* (n 11) 98-99.

²⁴ *Ibid* 104-05.

²⁵ *Ibid* 112.

²⁶ William A Reese Jr & Michael S Weisbach, 'Protection of Minority Shareholder Interests, Cross-Listings in the United States, and Subsequent Equity Offerings' (2002) 66 *Journal of Financial Economics* 65, 86, 101-02.

²⁷ *Ribstein* (n 11) 109.

companies, for example, tend to come from countries where investor protection is weakest.²⁸ This observation might appear counter-intuitive because FPIs from weakly regulated countries would have to spend more resources to raise their standards high enough to cross-list. It is precisely those companies, however, which have the most to gain from cross-listing and most need to signal to investors that they are of higher quality than other companies from their jurisdiction.

Anecdotal evidence of bonding and signaling comes from statements made by delisting firms. When some companies deregister from the SEC, they make a point to emphasize that although they will no longer be required to meet the regulatory requirements of the U.S. Securities Exchange Act, they will remain subject to high regulatory standards in their home country. When Naspers Limited, a South African company, delisted from NASDAQ, it stated that it would still be subject to the JSE's listing standards, South Africa's corporate governance guidelines, and South African law. When Telenor ASA, a Norwegian telecommunications firm, delisted from NASDAQ, it explained that all of its investors would obtain the protections afforded by the Oslo Stock Exchange and Norwegian law.²⁹ These and other companies that choose to delist want to signal their continued high quality to investors, notwithstanding their decision to end compliance with Sarbanes-Oxley.

D. Extraterritorial Application of U.S. Law

²⁸ Ibid 106 (quoting *Reese & Weisbach* (n 26)).

²⁹ See Dominic Jones, 'Foreign Firms Check Out of SEC's "Hotel California"' (Investor Relations Web Report 30 May 2007) <<http://www.irwebreport.com/daily/2007/05/30/foreign-firms-check-out-of-secs-hotel-california>> accessed 30 March 2008.

Consistent with the bonding thesis, when FPIs register with the SEC and sell shares or Level 2 or 3 ADRs to U.S. investors, they generally subject themselves to the full panoply of the U.S. federal securities laws. This parity of treatment for non-U.S. firms contrasts with less stringent treatment other countries accord to foreign issuers. In many countries, listing requirements for foreign issuers are less burdensome than those applied to domestic firms.³⁰ The SEC has made some exceptions for foreigners, but not many. FPIs, for example, are not required to file quarterly reports with the SEC.³¹ Until recently they were not required to file on the SEC's EDGAR system.³² And FPIs can file their financial statements with the SEC using International Financial Reporting Standards developed by the International Accounting Standards Board, as opposed to adhering to US GAAP.³³ Most other provisions of the securities laws, however, apply equally to FPIs.

When Sarbanes-Oxley was passed, and Congress provided no general exception or exclusion for FPIs, the FPI community reacted negatively. In letters to the SEC commenting on proposed rules to implement Sarbanes-Oxley, foreign governments and representatives of foreign firms objected to the extraterritorial application of the law.

³⁰ See *Coffee* (n 11) 239 n 20.

³¹ See Exchange Act Rule 13a-13, 17 CFR s 240.13a-13 (2007).

³² Mandated Edgar Filing for Foreign Issuers, Securities Act Release No 8,099, Exchange Act Release No 45,922, International Series Release No 1,259, 67 Fed Reg 36,678 (14 May 2002).

³³ Acceptance From Foreign Private Issuers of Financial Statements Prepared in Accordance With International Financial Reporting Standards Without Reconciliation to U.S. GAAP, Securities Act Release No 8,879, Exchange Act Release No 57,026, International Series Release No 1,306, 73 Fed Reg 986 (4 January 2008).

Japanese authorities, for example, raised “serious concerns” with respect to the application of the law to Japanese firms and urged that the problems addressed by Sarbanes-Oxley be handled by cooperation between the United States and foreign authorities.³⁴ The British argued that the SEC should adhere to its policy of deferring to foreign laws with respect to corporate law and corporate governance, given the overlap between local laws and Sarbanes-Oxley.³⁵ The Swiss argued more strenuously that application of Sarbanes-Oxley would be inconsistent with foreign law and conflict or unduly interfere with the internal operations and obligations of foreign private issuers.³⁶

When the SEC believed that application of rules adopted under Sarbanes-Oxley would directly conflict with a FPI’s home country’s law, it provided relief to avoid the conflict. One example is the rule adopted under section 307 of the Act, which required the SEC to prescribe minimum standards for attorneys appearing and practicing before it. The rule requires an attorney to report evidence of certain violations of law “up-the-ladder” within the company to the chief legal officer, chief executive officer, or an equivalent officer, and, if they do not respond, to the audit committee or the full board. Many non-U.S. attorneys complained that reporting under this requirement would be

³⁴ Letter from Hideo Hato, Director for Corporate Accounting and Disclosure, Japanese Financial Services Agency (SEC Comment letter 19 August 2002) <<http://www.sec.gov/rules/proposed/s72102/hhato1.htm>> accessed 30 March 2008.

³⁵ Letter from Peter Maynard, Group Legal Services Director, Prudential PLC (SEC Comment letter 19 August 2002) <<http://www.sec.gov/rules/proposed/s72102/pmaynard1.htm>> accessed 30 March 2008.

³⁶ Letter from Arnold Knechtle, Director, and Christian Stiefel, Legal Counsel, Federation of Swiss Industrial Holding Companies (SEC Comment letter 19 August 2002) <<http://www.sec.gov/rules/proposed/s72102/aknechtle1.htm>> accessed 30 March 2008.

inconsistent with their home country law.³⁷ Thus, in the final rule, the SEC stated that a non-U.S. attorney “shall not be required to comply . . . to the extent that such compliance is prohibited by applicable foreign law.”³⁸

This specialized treatment, however, was not the norm. Although some consideration was given to exempting foreigners from provisions of Sarbanes-Oxley, those efforts largely failed and FPIs must satisfy almost all provisions of the statute. FPIs registered with the SEC are subject, for example, to the same section 302 certification requirements and the section 404 annual assessment of internal control requirements as other issuers. The only difference is that since FPIs do not file quarterly reports, the evaluation must only be done at the end of each fiscal year.³⁹ FPIs were required to comply with the section 404 assessments with the first report filed for the first fiscal year ending on or after July 16, 2006.

FPIs were particularly concerned about the application of Sarbanes-Oxley because they felt trapped in a system from which they could not escape. Until recently, although it was relatively simple for a FPI to access the U.S. markets, it was often almost impossible to leave. SEC Chairman Cox referenced the 1970s Eagles song “Hotel California,” agreeing that foreign firms often could “never leave” even if they wanted to.

³⁷ See, eg, Letter from Tohru Motobayashi, President, Japan Federation of Bar Associations (SEC Comment letter 31 March 2003) <<http://www.sec.gov/rules/proposed/s74502/tmotobayashi1.htm>> accessed 30 March 2008.

³⁸ 17 CFR s 205.6(d).

³⁹ 17 CFR s 240.13a-15(b)(1); 17 CFR s 240.15d-15(b)(1).

Cox said that this was a great song, but a bad business model.⁴⁰ As a result, the FPI community viewed the application of Sarbanes-Oxley to non-U.S. firms as unfair. If a FPI had registered with the SEC before the passage of Sarbanes-Oxley, that decision presumably was based on a cost-benefit determination shorn of the burdens imposed by the Act. Since a decision to register could not be easily reversed, the inability to leave exacerbated the frustration of foreign firms that had to comply.

In March 2007, the SEC adopted revised rules to remove barriers to deregistration and delisting. Under the old rules, to deregister and delist, a FPI would have to show it had a low number of U.S. shareholders, or a decrease in the amount of its U.S. public float. Under the new rules, a FPI may terminate its SEC registration under section 12(g), or its reporting obligations regarding a class of equity or debt securities under section 15(d), rather than just suspending those obligations, based on low trading volume.⁴¹ Although under the new rules FPIs will not be wedded to the U.S. markets if they want to exit, those rules do not address underlying concerns that the Act has made the U.S. markets substantially less competitive.

E. Competitiveness of the U.S. Markets

The debate over the effects of Sarbanes-Oxley on markets has become as important as the debate over the effects of the Act on issuers. The Committee on Capital

⁴⁰ Christopher Cox, SEC Chairman, 'Opening Remarks at Open Meeting' (Speech at a meeting of the Securities and Exchange Commission 14 December 2005)

<<http://www.sec.gov/news/speech/spch121405cc.htm>> accessed 30 March 2008.

⁴¹ Termination of a Foreign Private Issuer's Registration of a Class of Securities Under Section 12(g) and Duty to File Reports Under Section 13(a) or 15(d) of the Securities Exchange Act of 1934, Exchange Act Release No 55,540, International Series Release No 1,301, 72 Fed Reg 16,934 (5 April 2007).

Markets Regulation Interim Report from November 2006, known as the Paulson Committee Report, notes that U.S. capital markets are losing competitiveness to foreign markets and that regulatory and legal costs play a role.⁴² Shortly after the release of the Paulson Committee Report, New York Mayor Michael Bloomberg and Senator Charles Schumer issued a report stating that New York's decline in competitiveness is attributable in part to concerns about compliance with section 404.⁴³ Even President Bush in his State of the Economy address in January 2007 noted that "complying with certain aspects of [Sarbanes-Oxley], such as Section 404, has been costly for businesses and may be discouraging companies from listing on our stock exchanges."⁴⁴ Similarly, many in the academic community have asserted that Sarbanes-Oxley has damaged the competitiveness of the U.S. markets.⁴⁵

I. Concerns About Market Competitiveness

Concerns about market competitiveness include three potential developments. First, issuers both in the United States and outside the United States contemplating a

⁴² Committee on Capital Markets Regulation, *Interim Report of the Committee on Capital Markets Regulation* (Report) (2006) 47.

⁴³ Michael Bloomberg and Charles Schumer, *Sustaining New York's and the US' Global Financial Services Leadership* (Report) (New York 2007) 12

<http://www.senate.gov/~schumer/SchumerWebsite/pressroom/special_reports/2007/NY_REPORT%20FINAL.pdf> accessed 29 March 2008.

⁴⁴ George Bush, 'State of the Economy Report' (Speech at New York's Federal Hall January 2007) <<http://www.whitehouse.gov/news/releases/2007/01/20070131-1.html>> accessed 29 March 2008.

⁴⁵ See *Davidoff* (n 11) 91; Robert DeLaMater, 'Recent Trends in SEC Regulation of Foreign Issuers: How the U.S. Regulatory Regime is Affecting the United States' Historic Position as the World's Principal Capital Market' (2006) 39 *Cornell International Law Journal* 109, 116.

public offering may choose London or Hong Kong over New York. Second, SEC registered and cross-listed firms may decide to give up their U.S. listing and exit the U.S. markets. Finally, concerns have been raised that the advantages to a U.S. listing – such as the premium FPIs enjoy as a result of cross-listing – will evaporate, which may fuel the first two concerns mentioned. We look at each of these concerns in turn.

The Paulson Committee Report emphasized the shift in attention away from U.S. markets to foreign markets and placed blame, at least in part, on overregulation. The Report contains figures on the increasing number of overseas IPOs and pointed out that London has begun to attract a greater share of IPOs from U.S. companies.⁴⁶ The Bloomberg-Schumer report noted that in 2006, U.S. exchanges attracted only one-third of the IPOs (by market value) that they attracted in 2001.⁴⁷ Even SEC Chairman Cox, in a 2007 interview, admitted that Sarbanes-Oxley caused many in the United States to look at opportunities on foreign markets.⁴⁸ Some evidence allegedly showed that the number of non-U.S. companies listing in the United States compared to U.S. companies listing declined after 2002.⁴⁹ And anecdotal evidence from issuers suggests they are looking at overseas markets as a way to avoid U.S. regulation.⁵⁰

⁴⁶ *Committee on Capital Markets Regulation* (n 42) 2-3.

⁴⁷ *Bloomberg and Schumer* (n 43) 12.

⁴⁸ Headliner Q&A, 'Getting it Right' (2007) 3 *Journal of Accountancy* 28, 29.

⁴⁹ Hong Zhu and Ken Small, 'Has Sarbanes-Oxley Led to a Chilling in the U.S. Cross-Listing Market?' [March 2007] *CPA Journal* <<http://www.nysscpa.org/cpajournal/2007/307/essentials/p32.htm>> accessed 29 March 2008.

⁵⁰ M Richtel, 'Looking for Best Place to Take a Company Public, Some Look Overseas' *The New York Times* (New York 22 December 2006) C5.

The potential shift to foreign markets is welcome news to foreign exchanges, which often promote a lower level of regulation abroad as a reason to list there. An official from the Toronto Stock Exchange stated that U.S. firms should look to the TSX as a potential market because it is more lightly regulated than the U.S. exchanges.⁵¹

In addition to the focus on whether U.S. and non-U.S. firms are deciding to list abroad as opposed to in the United States, some have focused attention on deregistrations and delistings. The number of FPIs that decided to deregister and delist allegedly began to increase around 2002, and the number of FPIs delisting increased relative to the number of U.S. companies delisting. Some concluded, therefore, that Sarbanes-Oxley caused the decision of FPIs to delist.⁵² Anecdotal reports from companies choosing to delist suggest that Sarbanes-Oxley is the culprit. Telekom Austria AG and Vernalis PLC, a British pharmaceutical company, referenced Sarbanes-Oxley as a reason for delisting.⁵³ More recently, U.K.-based BioProgress PLC, Norway-based Petroleum Geo-Services ASA, and the Israeli company Koor Industries Limited, all cited the high costs of complying with the Exchange Act as a reason to delist and deregister.⁵⁴

II. Responses to Concerns About Competitiveness

Others take a different view and, over the last several years, a pro-regulatory response has emerged. In a presentation shortly before he left the Commission, former

⁵¹ Rachel McTague, 'At ABA Meeting, TSX, UK Lawyer Solicit Foreign Stock Exchange Listings' (2007) 39 Securities Regulation & Law Report 1275.

⁵² *Zhu and Small* (n 49).

⁵³ P Stiff and R Stone, 'British Airways Approves Delisting From NYSE as More European Firms Tire of U.S. Rules' *Wall Street Journal* (New York 26 April 2007) C3.

⁵⁴ *Jones* (n 29).

SEC Commissioner Roel Campos stated that he believes regulation is a competitive *advantage* for the U.S. markets. Commissioner Campos explained that the U.S. share of IPOs declined before 2002 and then increased in 2005, and much of the decline in foreign listings in 2005 (15 of 26) was due to mergers and acquisitions. Sarbanes-Oxley, therefore, cannot be blamed.⁵⁵ PCAOB member Charles Niemeier similarly disputed statements in the Paulson Committee Report and the Bloomberg-Schumer report stating that research in the area of market competitiveness does not support findings that regulation is hurting competition. Rather, enhanced regulation, such as Sarbanes-Oxley, is attractive because of investor protections afforded by the new law and a consistent premium for issuers subject to it.⁵⁶

More recently, former Senator Paul Sarbanes, a primary sponsor of the Sarbanes-Oxley Act, told a Rutgers University audience that regulation of the Sarbanes-Oxley variety is a competitive advantage.⁵⁷ French economic minister, Christine Lagarde, agrees, stating that the “security and solidity” of the French regulatory system was a strength for competitiveness and that any reforms should be in the area of taxation.⁵⁸

Recent research suggests that these individuals may be right. According to the pro-regulatory view, enhanced regulation and enforcement activity yield higher valuation of securities and a lower cost of capital. As discussed, managers agree not to appropriate

⁵⁵ Roel Campos, ‘Speech by SEC Commissioner: Remarks Before the Consumer Federation of America Financial Services Conference Speech to CFA’ (Speech December 2006)

<<http://www.sec.gov/news/speech/2006/spch120106rcc.htm>> accessed 29 March 2008.

⁵⁶ Cutler (n 11).

⁵⁷ P Sarbanes, ‘Regulating Business in the 21st Century: The Case of Sarbanes-Oxley’ (Speech April 2008).

⁵⁸ B Hall, ‘Paris Covets First-Tier Status’ *Financial Times* (London 5 October 2007) 3.

private benefits by subjecting themselves to stringent regulation, such as SEC enforcement and private investor lawsuits. As a result, the market responds favorably to such firms compared to those where managers do not agree to forgo such benefits.⁵⁹ The Federal Reserve Bank of New York released a report earlier this year concluding that at least with respect to the U.S. equity markets, U.S. competitiveness has not suffered.⁶⁰ Moreover, the market share of non-U.S. companies listing on U.S. exchanges as opposed to the London Stock Exchange has increased from 1998 to 2005.⁶¹

In addition to information regarding the number of listings or delistings, others have studied the share price premium obtained by FPIs who choose a U.S. listing. By examining a ratio known as Tobin's q, which compares the market value of a company's stock to the asset value of the firm, researchers have observed that FPIs with shares cross-listed in the United States enjoy a significant premium compared to non-U.S. issuers from the same country, which do not cross-list.⁶² Kate Litvak, however, has found that the premium for FPIs cross-listed in the United States and subject to Sarbanes-Oxley has

⁵⁹ See *Coffee* (n 11) 285.

⁶⁰ Stavros Peristiani, Federal Reserve Bank of New York, 'Evaluating the Relative Strength of the U.S. Capital Markets' (Report) (2007) 13 Current Issues on Economics and Finance <http://www.newyorkfed.org/research/current_issues/ci13-6.html> accessed 4 April 2008.

⁶¹ Craig Doidge et al, 'Has New York Become Less Competitive in Global Markets? Evaluating Foreign Listing Choices over Time' (2007) 4 Charles A. Dice Center for Research in Financial Economics Working Paper No. 9/2007 <<http://ssrn.com/abstract=982193>> accessed 29 March 2008 (Dice Center Working Paper 9/2007).

⁶² *Doidge et al* (n 20) 205, 206.

declined relative to the premium for FPIs who have accessed the U.S. markets but are not subject to the new law.⁶³

Supporters of Sarbanes-Oxley point out that establishing a cross-listing in the United States still results in a premium, whereas cross-listing in the U.K. results in none.⁶⁴ They also point out that the drop in the number of U.S listings and the decline in valuations occurred before the advent of Sarbanes-Oxley. SEC Chairman Cox made this point to the U.S. Chamber of Commerce in a conference on competitiveness in early 2007. He noted that the decline in the U.S. market share for listings predates Sarbanes-Oxley and hypothesized that other factors caused the decline, such as the new opportunities for global listings.⁶⁵ According to one recent study, cross-listing premia actually declined in the period 2000-2001 before the passage of Sarbanes-Oxley, increased in 2003 and then stabilized.⁶⁶ Thus, researchers reviewing the empirical evidence are unable to draw firm conclusions as to what the data shows.⁶⁷

John Coffee asks why any FPI would delist if a premium for cross-listing in the United States remains?⁶⁸ Perhaps the answer is that the overall costs of staying listed are not worth the benefits. Coffee puts forward the potential rationale that the benefits of a

⁶³ *Litvak* (n 18) 1860-61.

⁶⁴ *Doidge et al* (n 61).

⁶⁵ Christopher Cox, 'Speech by SEC Chairman: Address to Joint Meeting of the National Endowment for Democracy and the Foreign Policy Association' (Speech March 2007)

<http://www.sec.gov/news/speech/2007/spch031407cc-2.htm>> accessed 29 March 2008.

⁶⁶ *Doidge et al* (n 61).

⁶⁷ See *Coffee* (n 11) 247 n 37.

⁶⁸ *Coffee* (n 11) 237.

valuation premium might be overridden by other factors, such as the control regained by controlling shareholders, which they relinquished with a cross-listing; a desire to avoid the application of new regulation; or fear of potential U.S. enforcement penalties. Coffee hypothesizes that the United States might be a magnet for *higher quality* issuers that will take advantage of lower costs of capital. It is this possibility – that lower quality issuers are leaving the U.S. markets and higher quality issuers are remaining – that we address below. If Coffee is right, then, as he states, the policy implications are significant and regulators should avoid reducing regulation because a reduction would reduce the bonding premium foreign firms obtain by cross-listing their shares and increase their cost of capital.⁶⁹

F. Literature review

Several studies have been performed over the past several years examining the effects of Sarbanes-Oxley on both U.S. issuers and FPIs. A number of studies focus exclusively on the effects of Sarbanes-Oxley on FPIs. Some researchers show that investors react negatively to Sarbanes-Oxley, calling into question benefits of cross-listing, such as the bonding premium discussed above. Other research tries to isolate the effects of Sarbanes-Oxley by doing a cross-regional analysis. Some researchers focus on listing and delisting decisions and certain research, similar to ours, examines which companies are more prone to deregistration and delisting and conclude that those firms with low turnover, poor performance, or other negative characteristics are more likely to give up their U.S. listing.

⁶⁹ Ibid 300.

Kate Litvak sought to test the validity of investors' views that Sarbanes-Oxley would negatively affect FPIs cross-listed in the United States that were subject to the new law.⁷⁰ She found that FPIs subject to Sarbanes-Oxley displayed negative returns as a result of certain events, such as Congressional action indicating an increased probability that the law would be enacted and would apply to FPIs. Almost every important announcement suggesting increased likelihood that the law would be passed was associated with a negative reaction to stock price in cross-listed companies compared with companies not cross-listed, and the one event suggesting a possible exemption for cross-listed companies was associated with a positive reaction.

Xi Li also examined the effect of Sarbanes-Oxley on cross-listed FPIs.⁷¹ Li compared the returns of cross-listed FPIs during a number of Sarbanes-Oxley legislative events from 1999 to 2003 against an index of those companies' home markets (excluding any FPIs) over the same time period.⁷² Li also discovered that the cross-listed FPIs with better corporate governance structures tended to respond more negatively to Sarbanes-Oxley regulation.⁷³ The study concluded that the costs of compliance with Sarbanes-Oxley for FPIs could significantly exceed the benefits and weaken existing benefits of legal bonding.⁷⁴

⁷⁰ Kate Litvak, 'The Effect of the Sarbanes-Oxley Act on Non-US Companies Cross-Listed in the US' (2007) 13 *Journal of Corporate Finance* 195.

⁷¹ Xi Li, 'The Sarbanes-Oxley Act and Cross Listed Foreign Private Issuers' (2007) (on file with author).

⁷² *Ibid* 1-2.

⁷³ *Ibid* 29.

⁷⁴ *Ibid*.

Similarly, Philip G. Berger, Feng Li, and M.H. Franco Wong found that FPIs had a negative valuation reaction to Sarbanes-Oxley compared with U.S. firms.⁷⁵ The authors interpret the negative reaction to mean that the marginal benefits of bonding for cross-listed firms were lower than the marginal costs imposed by Sarbanes-Oxley. These researchers predict an inverse relation between the response to Sarbanes-Oxley and level of investor protection in a company's home country – and a positive relation between reaction to the law and a FPI's growth potential. The results were consistent with Sarbanes-Oxley being more beneficial to FPIs from countries where investor protections are weaker.

Christopher Woo performed a regional analysis. He conducted a survey of issuers from twelve jurisdictions to measure the effects of Sarbanes-Oxley on the quality of the companies from particular regions listing in the United States.⁷⁶ Examining data from the point of view of both trading volumes and market capitalization, Woo concludes that the U.S. markets are important to companies in Latin America and Israel and that any increased regulation will not result in a decrease in listings from those areas.⁷⁷ Woo notes, however, that issuers from Japan, Australia, and Europe, with more robust disclosure rules, may be more inclined not to list in the United States.⁷⁸

⁷⁵ Philip Berger, Feng Li & MH Franco Wong, 'The Impact of Sarbanes-Oxley on Cross-listed Companies' (2005) University of Chicago Working Paper (on file with author).

⁷⁶ Christopher Woo, 'The Effects of the Sarbanes-Oxley Act on Foreign Private Issuers' (2003) (on file with author).

⁷⁷ Ibid 60.

⁷⁸ Ibid.

Geoffrey Peter Smith also examined effects of Sarbanes-Oxley on cross-listed firms.⁷⁹ Smith reviewed the differential response between firms affected by Sarbanes-Oxley and OTC counterparts not affected by the statute. Smith also looked at new cross-listing and delisting activity surrounding Sarbanes-Oxley. Smith finds an overall negative response to new rules with respect to stock price. New cross-listings fell, but delistings were steady – although a greater percentage of delistings (37% as opposed to 18%) were voluntary.

Some studies have looked specifically at a firm’s decision to list and delist. Craig Doidge, G. Andrew Karolyi, and Rene M. Stulz analyzed the argument that Sarbanes-Oxley has discouraged foreign listings due to the costs imposed.⁸⁰ The authors assert that this argument can only be supported if firms that would have listed in the United States in the 1990s would not do so now.⁸¹ The authors found scant support for this proposition, and uncovered little evidence to show that listing decisions have changed in the aftermath of Sarbanes-Oxley.⁸² Instead, the authors concluded that the only change is that non-listed firms tend to be smaller and therefore less likely to list on major exchanges.⁸³

Jon Witmer examined why foreign companies decide to delist from U.S. exchanges.⁸⁴ Witmer observed the characteristics of firms that voluntarily delist—

⁷⁹ *Smith* (n 18).

⁸⁰ *Doidge et al* (n 61) 1.

⁸¹ *Ibid* 42.

⁸² *Ibid*.

⁸³ *Ibid*.

⁸⁴ Jon Witmer, ‘Why Do Firms Cross-(de)list? An Examination of the Determinants and Effects of Cross-delisting’ (2005) 2 Queen’s University Preliminary Draft (on file with author).

finding that smaller firms with a lower percentage of turnover in the United States are more likely to delist.⁸⁵ In addition, Witmer noted that firms are more likely to cross-delist if they are from countries with less investor protection or if they listed after Sarbanes-Oxley was passed.⁸⁶ Witmer acknowledged that these findings support the hypothesis that the added expense of U.S. regulation has led to increased delisting.⁸⁷

Work by Susan Chaplinsky and Latha Ramchand is perhaps the most similar to ours, comparing delisted and stay-listed firms to isolate the characteristics of each.⁸⁸ The authors examined listings and delistings of non-U.S. firms over a 44 year period (1961-2004) to determine whether the stay-listed firms were of higher quality than the delisted firms. They found that those companies that voluntarily delisted had low profitability, median assets and market capitalization of less than \$230 million, a declining share price by 54% from listing to delisting, and 60% had no analyst coverage within a year following its listing. The authors conclude that these companies suffered from poor quality and low investor recognition. They contend that regulatory costs alone cannot explain the delistings. Rather, the exit is better explained because the firms were not viable candidates for listing in the first place.

Our work differs from Chaplinsky's and Ramchand's in a few respects. First, their data ends in 2004, two years after the passage of Sarbanes-Oxley and before some of the rules implementing the statute were effective. Our data includes the years 2005

⁸⁵ Ibid.

⁸⁶ Ibid.

⁸⁷ Ibid.

⁸⁸ Susan Chaplinsky and Latha Ramchand, 'From Listing to Delisting: Foreign Firms' Entry and Exit from the U.S.' (2007) (on file with author).

and 2006. Second, in addition to examining return on assets, we measured return on equity and profit margin as well, providing a different basis on which to assess the financial profile of the deregistering firms.

G. Methodology and Preliminary Results

This section explains our methodology and preliminary results. We reviewed the financial profile of deregistered and stay-registered firms from four countries over a seven year period. Although our results are preliminary, the data show a clear trend: deregistering firms have substantially weaker performance compared to those firms that stay registered. This data calls into question the widely held assumption that the costs of regulation alone are causing FPIs to deregister. If our results are replicated with additional study, it appears that poor performance, not necessarily regulatory costs, is driving certain FPIs from the U.S. markets.

To begin to understand why FPIs might want to delist and deregister, we first set out to understand the financial profile of those companies that actually deregistered from the SEC. (Registration and reporting are preconditions to listing on a U.S. exchange.) What distinguishes the deregistered from the stay-registered companies? To answer that question, we examine and evaluate the performance profitability profile of the deregistered companies compared to those that have not deregistered. We focus not on the effects of Sarbanes-Oxley on deregistered firms, rather, we examine their financial profitability profile.

We review data for firms over a seven year period, beginning in 2000, before the passage of Sarbanes-Oxley, to determine whether deregistered firms had differential performance when compared to the stay-registered firms. We limited ourselves to

collecting data from four countries, Great Britain, France, Germany, and Italy, as a pilot study to determine whether further research is warranted.

We used data from the U.S. SEC and from Datastream. The SEC's Division of Corporation Finance maintains a database of international registered and reporting companies.⁸⁹ International registered and reporting companies are FPIs subject to the SEC registration and reporting requirements under the Securities Exchange Act of 1934. We included FPIs in our analysis if they appeared on the SEC database and company information was available in Datastream. We considered a company to be a delisting firm if, during the period examined, the company dropped off of the SEC's database of registered and reporting companies, in other words, if it appeared in the database for one year but not the next. We considered a company a stay-registered firm if it remained in the database for all years 2000-2006, or from the first year it appeared through 2006.

As of the time of writing, 2007 data is not available. The lack of 2007 data is unfortunate for a number of reasons. First, as discussed, the SEC recently eased the burden on FPIs seeking to deregister from the SEC. Those rules first became effective in 2007. As a result, pent up demand for deregistering may have led to a large number of companies deregistering in 2007 and, therefore, inclusion of the 2007 firms would enhance our data set. Second, as mentioned, in some cases, SEC registrants were required to comply with the provisions of section 404 with their first report filed for the fiscal year ending on or after July 16, 2006. Since FPIs typically do not file quarterly reports, many FPIs were required to make their first filing under the section 404 rules

⁸⁹ Available at <<http://www.sec.gov/divisions/corpfin/internatl/companies.shtml>> accessed 21 April 2008.

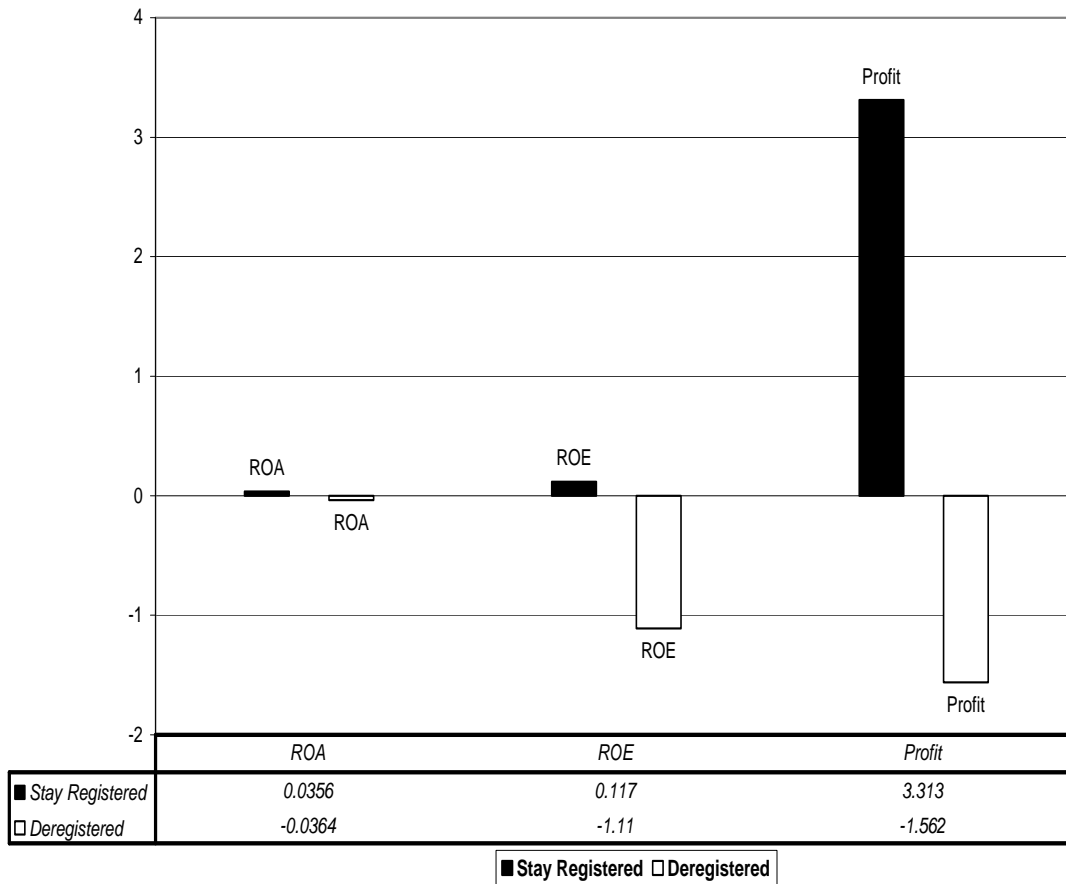
during 2007. It is possible that certain FPIs deregistered in time to avoid meeting that requirement and we would want to include those firms in our data.

Our preliminary data consists of information from 139 firms: 70 from Great Britain; 32 from France; 24 from Germany; and 13 from Italy. Of the total 139 firms, 56 deregistered. The breakdown of deregistering firms by country is as follows: for Great Britain, 36 of the 70 deregistered; for France 12 of 32 deregistered; for Germany, 6 of 24 deregistered; and for Italy, 2 of 13 deregistered. (We have not included country specific results for Italy given the relative small sample size. The overall trend found in the other samples, however, also is exhibited in the Italian firms.) Once we created the FPI database, we obtained relevant financial data from Datastream for the period 2000 to 2006, including total assets, total debt, total equity, net revenues, earnings per share, and number of shares outstanding. We were then able to calculate average return on assets (“ROA”), average return on equity (“ROE”), and average profit margins for the deregistered compared to the stay-registered FPIs.

The data across all firms indicate a wide range of profitability. ROE ranged from a minimum of -150% to a maximum of 11%. The skewed ROE distribution generated an average ROE of -0.33% across all firms and time. Average profitability, as a proportion of net revenues was 1.57%, and its standard deviation of slightly greater than 36% is indicative of a substantially heterogeneous profit margin picture. ROA exhibited a much tighter range of values, with a mean of 0.1%, and a standard deviation of 0.16%. The deregistered firms, however, had worse performance than the stay-registered firms. The deregistered mean ROE was -1.11%, profit margin was 1.56%, and the ROA was -0.03%. The stay-registered sample indicated an average ROE of 0.12%, mean profit margin of

3.31%, and average ROA of -0.04%. Statistical tests of difference in means indicated each difference significant at 5% or better. A graphical representation of the differences in performance profile can be found in Figure 1.

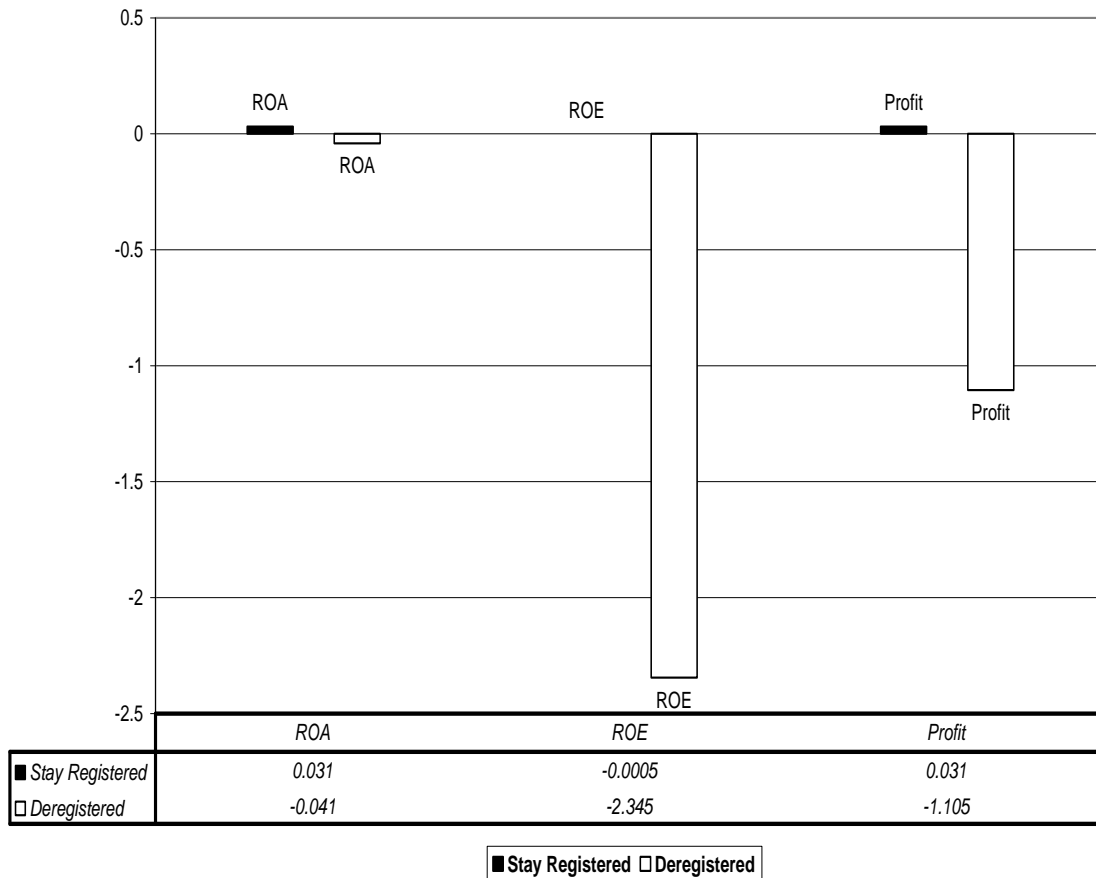
Figure 1
Performance Ratios - All Firms



French firms also exhibited poorer profit performance associated with the deregistered firms. For the deregulated firms, average ROA was -0.04%, mean ROE was -2.34%, and average profitability was -1.11%. The associated figures for the stay-registered sample were 0.03% for ROA, approximately 0% for ROE, and 0.03% for profit margin. Although there was no statistical difference between the ROE averages,

difference in means tests for ROA and profit margin indicated significance at the 5% or better level. Given the large ROE deviation between the registered and deregistered sample, the lack of significance in the difference may be surprising. The substantial variation in deregistered data for the French firms is one explanation. A graphical presentation of the differences is presented in Figure 2.

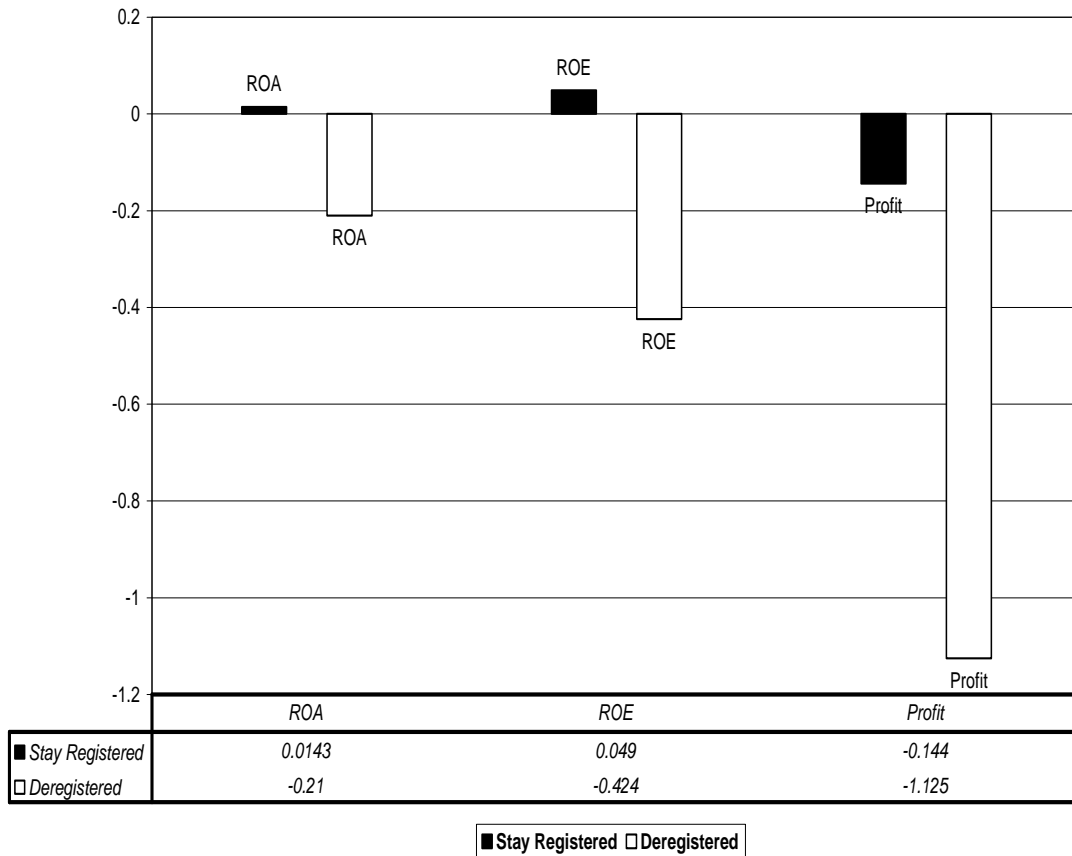
Figure 2
Performance Ratios - French Firms



The pattern of relative underperformance continues with the German firms choosing deregistration. Mean ROA was -0.21%. Average ROE was -0.42%, and average profitability was -1.13% for the deregistered sample. For the stay-registered sample, mean ROA was 0.01%, average ROE was 0.05%, and average profitability was -

0.14%. Differences in mean tests indicated ROA difference was significant at the 1% level, while ROE difference was significant at the 10% level. Profit margin difference was not found to be significant in the German firms. A graphical representation of these results is found in Figure 3.

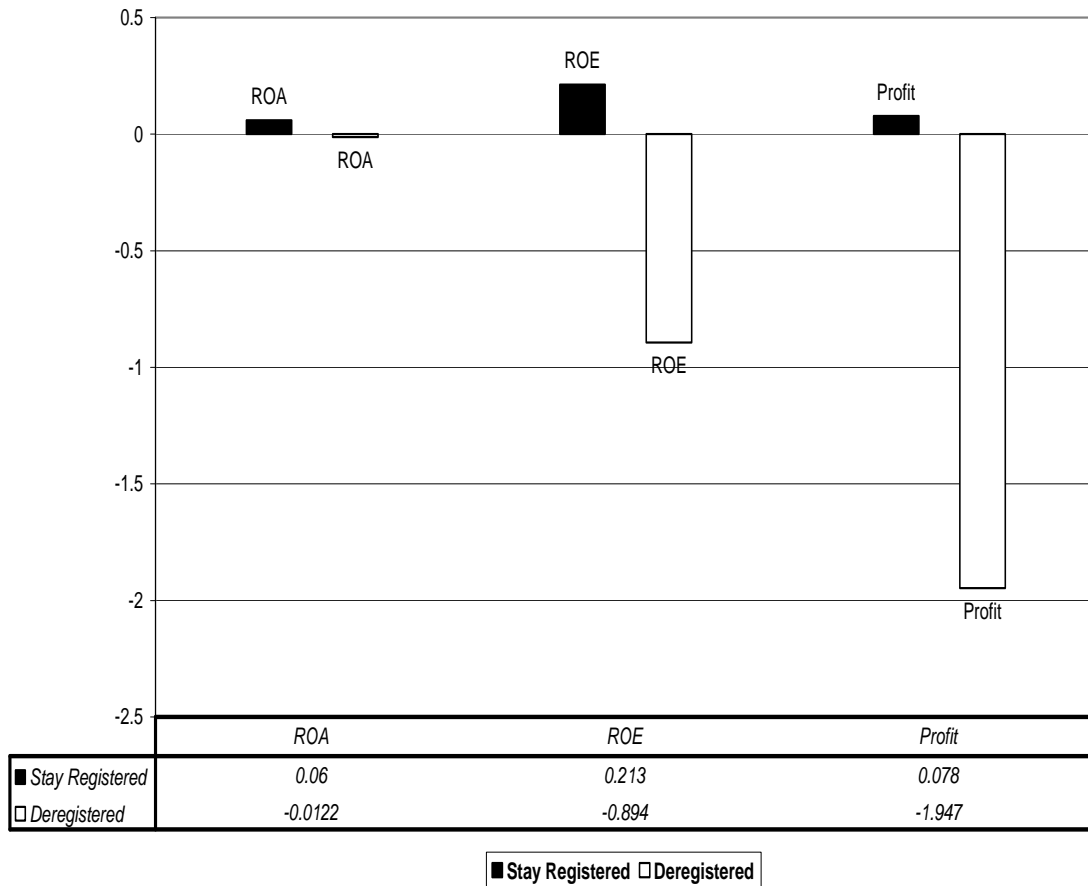
Figure 3
Performance Ratios - German Firms



The country with an almost even number of deregistered and stay-registered firms is the United Kingdom. As a reminder, of the 70 U.K. firms across the sample period, 34 firms stayed registered, while 36 chose to deregister. The profit underperformance trend for the deregistered firms is repeated in the U.K. sample. Average ROA was calculated to be -0.01%, mean ROE was -0.89%, and profit as a proportion of sales was -1.95% for

the deregistered firms. The stay-registered sample generated the following data: average ROA of 0.06%, mean ROE of 0.21%, and average profit margin of 0.08%. Differences between ROE and profitability were significant at the 10% or better level, while ROA difference was significant at better than the 1% level. The graphical representation of the deregistered and registered samples for the U.K. firms can be found in Figure 4.

Figure 4
Performance Ratios - UK Firms



Although the analysis at this stage evaluated a small slice of financial profile or financial performance measures, the profitability differences between registered and deregistered firms is consistent in the aggregate, as well as at the country level. Simply

stated, those firms choosing deregistration appear to be relative underperformers, at least in comparison to firms that decide to stay registered. Although the results are preliminary, and limited at this stage by the small number of countries examined and variables used, the differences between stay-registered and deregistered firms are significant and warrant additional investigation. If additional research is consistent with these results, the reasons for deregistration may have more to do with performance and other factors than with regulatory requirements. At this stage, there appears to be a connection between underperformance and registration status that calls for additional investigation.

H. Conclusion

Ever since early evidence suggested that Sarbanes-Oxley might be jeopardizing market competitiveness by making the U.S. exchanges less desirable for FPIs, academics and policy-makers have explored the effects of the new law on firms' decisions to register or deregister their shares in the United States. The reasons FPIs make such decisions are complex and, in most cases, a combination of factors is likely to be at work. Yet gaining a better understanding of such decisions is important. Calls for deregulation, while potentially attractive as a means to encourage more FPIs to list their shares in the United States, might be wrong-headed if based on a false assumption that the reason FPIs deregister is to avoid the burden of new regulations.

We have attempted to examine one aspect of FPIs' decisions to deregister from the SEC. The data we have gathered so far indicate that the FPIs that deregister are by and large poor performing firms – they have relatively low return on assets, return on equity, and profit margins. Our data is preliminary, but if the data is replicated when

additional countries are examined, then the basis for deregistering and delisting may have little to do with over-regulation and more to do with failure in performance.