

MEMORANDUM

March 24, 1965

Re : Trends in Financial Disclosures of Foreign Companies
 By : Maxwell Kaufman

In order to determine whether there has been any trend in recent years in financial disclosures of foreign companies and the nature thereof, I have examined various books, periodicals, exchange documents, memoranda and letters received by the staff in connection with our study of the foreign securities problem posed by Section 12(g) of the Exchange Act. This material indicates that the trend is towards improvement in the amount and availability of disclosure although specific documentation is generally not given. I have quoted or summarized below in chronological order pertinent portions of this material, indicating the source. In addition, I have appended a summary of the results of a study made by Ralph E. Eyster of changes in disclosure in material filed with the Commission by certain foreign issuers. A bibliography of material on foreign portfolio investments which was examined in connection with the preparation of this memorandum or which is otherwise pertinent to the foreign securities problem is also appended.

From Raymond L. Larcier, "European Common Stocks," The Analysts Journal, May 1959:

In discussing the control of new issues of shares in Belgium, the author states that the Belgian Banking Commission "sees to it that subscribers are not misled either as to the nature of

the undertaking or the rights pertaining to these shares. The Commission's activities in this field are aimed at promoting a gradual improvement in the contents of company prospectuses."

Referring to annual reports, he states that in Germany "in the matter of balance sheets, an increasingly large number of companies whose shares are widely owned by the investing public, go beyond the legal requirements and publish consolidated balance sheets." In France, "considerable efforts have been made by several companies to improve their annual reports, and the 'Chambre Syndicate' has insisted for several years on the need to increase the contents of such reports." Also, in France, "a new law has recently come out in pursuance of which companies must now give information about their turnover and their investment portfolios, as well as publish semi-annual reports." In Holland, "certain big international companies have published detailed information: quarterly reports, consolidated balance sheets, etc. Other domestic companies limit themselves to the publication of rather schematic annual reports complying with the requirements of the local Chamber of Commerce. The Association of Stockbrokers (Vereeniging voor de Effectenhandel) is trying to induce these companies to improve their annual reports."

Referring to the Common Market countries, Larrier states while efforts are being made (in order to have the shareholders better informed) such efforts are almost fruitless in some countries and very successful in others."

From Frances Haidt, "Analysts Explore European Investments," The Analysts Journal, July 1959:

Discussing a European field trip made by members of the New York Society of Security Analysts, the author states that "in practically all instances we received more information / from companies visited / than we had expected -- more than had previously been made available." The author refers to "management's willingness to meet with United States Analysts" and in outlining corporate information of interest to analysts mentions "that the reception accorded the New York Society of Security Analysts by the 30 European companies was so remarkable as to the amount of corporate information disclosed,"

From T. R. Lilley, "European Equities for the American Pension Fund," The Analysts Journal, July 1959:

Reporting on the same European trip mentioned in the preceding citation: "There is evidence, however, that the amount of information being made available by European firms is increasing. The inter-

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Wherever we visited on our trip, company officials were cooperative. Furthermore, modest but significant moves toward changing applicable laws are being made. In Germany, for example, we learned of a proposed change in the corporation law to broaden materially the requirements for corporate reporting."

From Ralph A. Roman, "The European Field Trip," The Analysts Journal,

July 1959:

Also with reference to the above mentioned field trip: "Surprising was both the quality and quantity of information the corporations gave us. . . . Another company gave us sales figures that had never before been released to the public."

"If there is to be widespread ownership, it is realized that there will have to be wider dissemination of information. The veil of secrecy regarding operations of European companies seems to be lifting, and many corporation officials expressed the belief that they will follow the steps of the American corporations in releasing more pertinent information to stockholders, Analysts and the press. Corporations are feeling their social responsibility today."

From Adolph E. Grunwald, "West German Stock Investment," The Financial

Analysts Journal, September - October 1960:

Discussing legally required improvements in the profit and loss statement of German companies: "With the recent passage of the 'Kleine Aktienrechts-reform' [Small Stock Reform Law], the German corporation is now required to report its net sales figure undebited by various other accounts, except price discounts and returns and allowances. This will enable the outside shareholder of West German firms, in the future, to make a more reasonable evaluation of the profitability and prospects for the enterprise."

From "Report of IFA Foreign Investment Committee," The Commercial and

Financial Chronicle, December 15, 1960:

Cautioning American investors, the Committee states: "Frequently, reading the balance sheet of a European company gives no real assurance as to the actual facts of financial strength or earning power. Annual reports are tardy and interim reports a rarity. A correction of this situation is of the utmost importance if Europe is to attract ownership capital from America on the scale justified by its economic potential. Some real progress has been made in this area in the last few years, and there is every indication that further progress will be made, particularly in Germany and France (under- scoring supplied).

Referring to annual reports in the United Kingdom, the Committee mentions that "companies are required to publish annual reports and they are publishing increasingly full information."

Yoshino

From Gakuzo, "Japanese Economy - New Market for Investors,"

Financial Analysts Journal, January - February 1962:

Describing the historical background, the author states: "The Tokyo Stock Exchange, which was closed by the Supreme Commander Allied Powers (SCAP) in 1945, reopened in May, 1949. Its operations, following the reopening, were based on a new Securities Exchange Law modeled after the 1933 and 1934 American Securities and Exchange Acts. Our Securities Exchange Law marked a new departure in Japanese investment since its major objective was the protection of stockholders."

From Paul A. Murphy, "Invest In Japan," Financial Analysts Journal,

May - June 1962:

Discussing the availability of investment information: "The MacArthur regime instituted many changes in Japan including a modified S.E.C. Stocks listed on the exchanges must file, for each six months period, a considerable amount of material, including sales by certain categories, costs, depreciation, selling and administrative expenses, corporate taxes and surplus reconciliation. A detailed balance sheet is also required. These are all available (in Japanese) about two or three months after the close of the period. Frequently there is more information than a similar American company would publish. In fact, Sony issues three reports; one to The Ministry of Finance (the commercial code), a second to the Tokyo Stock Exchange (a kind of 10K), and a third by Price Waterhouse (consolidated) - all somewhat different.

"The four leading Japanese security houses (Daiwa, Nikko, Nomura and Yamaichi) translate and publish this material as well as industry and economic studies. Since all four firms have New York and West Coast offices, this material is readily available."

From George Bookman, "An Accent on Foreign Stocks," Fortune,

July 1962:

Following a discussion of the ambiguities about profits in European financial reports and the use of hidden reserves, the author states that "Bit by bit, European corporations, sometimes prodded by their governments, are issuing more information, and are adopting accounting methods more like those used in the U.S.; and as they

become more interested in cultivating the American capital market, and in broadening share ownership in their own countries, this policy of disclosure will doubtless be extended."

From Harry G. Guttmann, "The Jenkins Report - British Corporation Law Scrutinized for Reform," Financial Analysts Journal, November - December 1962:

In Great Britain, a "14-member Company Law Committee, under the chairmanship of the distinguished jurist, Lord Jenkins, was appointed in December 1959 and released its report in June of this year / 1962 /. Its assignment was to review corporate practice and law and recommend changes. The / British / Companies Act was last overhauled under a Labour Government in 1948 after a similar study by the Cohen Committee."

"The importance of adequate disclosure is reflected in the space devoted to it in the two longest chapters. These are Chapter X on 'Accounts' and Chapter VII on 'The Protection of Investors,' and constitute more than a fourth of the book's length."

(Note: No attempt is made in this memorandum to summarize the Jenkins Report because of the magnitude of the study which covers 223 pages and contains 334 recommendations. The report is discussed in the memorandum dated December 14, 1964 prepared by Jeffrey D. Bauman re Legislative History of the Problem of Requiring Issuers of Foreign Securities Traded Over-the-Counter to Comply with the Disclosure Requirements of the Securities Exchange Act of 1934 and his memorandum of March 19, 1965 re Foreign Disclosure and Reporting Requirements. Among the principal recommendations are (1) sales figures, called "turnover," should be disclosed; (2) the publication of a five-year summary of important accounting figures; (3) the placing of "reserves" under accounting headings that will show their true nature; and (4) the giving of more adequate protection to investors with respect to take-over bids.)

From "Europeans Urge New Stock Rules," The New York Times,

June 7, 1963:

"The International Federation of Stock Exchanges unanimously agreed today that greater disclosure of financial information by listed companies was desirable to increase public interest in securities.

"The federation, a successor to the Association of European Stock Exchanges, agreed to 'study the object and the means of a concerted information policy.'

"The policy would touch such matters as improved company reports, consolidated balance sheets of multiple enterprises, publication of the investments of enterprises and more frequent publication of reports by companies.

"The issue of disclosure of financial information is an acute one in Western Europe. Today's resolution puts the European stock exchanges on record as favoring greater disclosure in principle.

* * *

"The federation includes the stock exchanges of Austria, Belgium, Britain, France, West Germany, Italy, Luxembourg, the Netherlands, Spain and Switzerland.

* * *

" . . . it was clear that the stock exchange representatives had agreed on the principle that more company information should be disclosed in Europe."

From "Second European Financial Analysts Congress - American Observers Report on Meeting; Financial Analysts Journal, September - October 1963:

The Second Congress of The European Federation of Financial Analysts Societies took place in Cambridge, England, in July 1963. American observers reporting on the meeting state: "Here was a diligent group of devoted men from several countries and all walks of financial life not trying (particularly at this time) to develop intricate techniques of analysis, but simply to arrive at the common ground of financial language terminology and concepts out of a relative morass of inadequate information."

The observers further state: "In the field of corporate reporting, major emphasis was placed upon the need for Analysts and Analyst Societies to push for better and more frequent reporting. It was felt that Analyst Societies rather than Analysts individually would be more successful, but it was also felt that the Federation itself should enter the arena and push its weight around." The observers go on to say that the keynote of the whole Congress was "an urgency to get things done and a will to lift the whole profession up by its own bootstraps."

From Manuel F. Cohen and Allen E. Throop, "Investment Of Private Capital In Foreign Securities" in Section V, "Financing Of International Business Transactions" in Walter S. Surrey and Crawford Shaw, editors,

A Lawyer's Guide to International Business Transactions (1963):

Discussing disclosure standards in foreign countries, the authors state that "Many countries appear to be moving in the direction of the United States standards. Since 1959, France has required that corporations whose securities are quoted on securities exchanges and which have assets in excess of one billion francs publish the amount of gross sales. Proposals for the disclosure of gross sales and costs of goods sold have been seriously advanced in England and in Germany. Under the impetus of the Common Market, further advances in the standardization of European accounting and disclosure practices may be expected. Other nations also have under consideration more comprehensive regulation of the offering and distribution of securities. These developments suggest that compliance with the standards embodied in the Securities Act will in the future present fewer problems than they do today." (Footnote references omitted.)

From Walter P. Stern, "Investing In Japan," Financial Analysts

Journal, January - February 1964:

In a section devoted to the investment climate in Japan, the author states that "Generally speaking, published material on the general economy, particular industries, and individual companies, is both freely available (although not always translated into English) and adequate by almost any standards."

Discussing Japanese accounting procedures, he states that "Reporting is generally rather detailed and presented in an acceptable form (although it should be reiterated that many companies do not publish statements in English so that a translation is sometimes necessary."

Commenting on income statement accounting, the author points out that "Income statements are generally complete in that they include sales, cost of goods sold, operating profit, non-operating profit, etc." With respect to balance sheet accounting, he indicates that "Balance sheets tend to be fairly accurate by usual American standards of accounting; consolidated statements; however, . . . are usually not given."

From Carl D. Ross, "The Changing Mexican Market," Financial Analysts

Journal, May - June 1964:

Discussing the wide variation in public disclosure of Mexican companies, the writer states, however, that "the situation is gradually improving and more companies are releasing more data than they did even five years ago." He goes on to point out that "A side effect of compulsory profit sharing has been to encourage some companies to disclose a profit and loss statement. The Bolsa / Mexico City

Stock Exchange⁷ is encouraging, but not compelling, release of quarterly financial statements, and an increasing number of listed companies are reporting quarterly earnings."

From Adolphe J. Warner, "H. 6793 - A Threat to U. S. Holders of Foreign Securities," Financial Analysts Journal, September - October 1964:

In arguing against the provisions of the Securities Acts Amendments of 1964 as they relate to foreign issuers, the author states that many foreign companies are gradually providing stockholders with more detailed information.

From Robert H. Jackson, "Public Offerings: A Comparative Study of Disclosure in Western Europe and the United States," Western Reserve Law Review, December 1964:

In contrasting Securities Act disclosure requirements and traditional continental business practices and accounting methods, the author concludes that "there is . . . an apparent growing tendency toward standardization of accounting disclosures and uniform business practices through the initial efforts of the Common Market Conferences, which should eventually enlarge the amount of information available to the prospective investor."

The final paragraph of his articles points out that "the Belgium securities regulations, the new French laws on stock exchange listings, and the modern Swedish law providing strict financial statements for public companies are great steps forward in giving the investor protection on new and subsequent issues."

From letter dated August, 1964, issued by the Chairman, London Stock Exchange, to companies listed on the Exchange:

The letter opens with the statement that "I feel sure that you will have noticed in recent years a growing volume of comment and public discussion as to the amount of information being made available by public companies to their shareholders. A number of companies already give much information in their annual reports and accounts and some publish quarterly or half-yearly statements. Such action has been greatly welcomed both as a contribution to the establishment of orderly markets and to the encouragement of public confidence."

The letter contains in an appendix a series of recommendations for further disclosure and draws particular attention to the following four points:

- "(a) the supplying of information as to the composition of a group of companies and as to any major interests in associated companies;
- (b) the disclosure of turnover;
- (c) where a company or a group carries on widely differing operations, the provision of an analysis of trading results;
- (d) the issue of quarterly or half-yearly interim reports."

The letter indicates that the Exchange proposes to make (a), (c) and (d) requirements for admission to quotation.

From Investors Chronicle, February 26, 1965, page 715 (as summarized in Jeffrey D. Bauman's memorandum of March 19, 1965 re Foreign Disclosure and Reporting Requirements):

The Exchange followed its August suggestions with more requirements for new companies. As of March 26, 1965, all new companies will have to give a supplemental undertaking to give a description of their different operations and the figures or percentages of these operations where material. In addition, the company must give the names and countries of its subsidiaries together with the percentage of the equity capital which it owns. When a company holds 25% of a subsidiary, it must give the particulars of the issued shares and loan capital and the reserves of the subsidiary. Finally, every new company must furnish its stockholders and the Exchange with a half-yearly interim report.

The Exchange noted that the response to its August 1964 letter had been very good and that many listed companies had voluntarily implemented some of its recommendations.

From a Resolution of The Federation Internationale des Bourses de Valeurs (Federation of International Stock Exchanges) released November 24, 1964:

This resolution is headed "Information for the Public on the Activities and Assets of Officially Quoted Companies," sets forth conclusions reached at a meeting of the Federation and recommends that member stock exchanges encourage the companies whose securities are quoted on their exchanges to comply with the conclusions. These conclusions cover 16 points of disclosure in the balance sheet, 11 in the profit and loss accounts including consolidated net external

sales, and 3 regarding consolidation of accounts. Disclosure of the following information is also called for: turnover, nature of activity and volume of production, technical activity, future programs, portfolio of investments, fixed investments, stocks (inventory), long and medium term debts, fiscal regulations and banking obligations. The resolution goes on to recommend the publication of semi-annual interim financial statements.

From "Swiss Companies - More Information?", The Economist, January 23, 1965:

The article states that "More companies are now giving details of their turnover - including three out of the four big chemical companies in Basle, * * *." The article also describes as an important step forward a circular sent to all Swiss companies which recommends that in the next few years companies with shares listed on the stock exchange should supply information about such matters as group turnover, and its geographical and product distribution; methods of valuation of assets and investment practices; and the presentation of comparative statistics over a period of years.

From Robert W. Gibson, "Comparative Professional Accountancy - Australia," The Accounting Review, January 1965:

This article outlines some significant changes which have occurred in the last five years in Australia with particular reference to the accountant's duties arising from the Uniform Companies Act adopted in 1961 by the six Australian States.

"The recent division of proprietary companies has increased to some extent the number of companies required to publish accounts. Amendments to the standards of disclosure have also been included in the Uniform Acts."

"Significant new items included in the minimum statutory disclosure include

- (i) Inclusion of the previous year's comparative figures.
- (ii) The aggregate quoted market value of any investments including government bonds and shares in companies listed on a stock exchange.
- (iii) The cost value and amount of depreciation provided to date for all fixed assets (a transition clause allows some existing assets to be carried forward at net book value).

- (iv) The amount outstanding on contracts for capital expenditure.
- (v) The balance of provision for taxation in addition to the amount provided in the particular year."

Companies which raise funds in any of the forms discussed in the article are now required to file a six-monthly Balance Sheet and Profit and Loss Account.

On September 1, 1964, the Associated Stock Exchanges issued a new 'Official List Requirements.' "A new requirement requires the accounting reports to be issued within four months of the close of the financial year." "Quarterly and half yearly reports from 'borrowing' companies will be required in all states . . ."

In the conclusion to his article, the author states: "The most significant change in Professional Accounting in Australia over the past five years has been the introduction of uniform legal requirements with respect to companies.

The scope of the auditor's duty has been extended by an increase in the range of companies required to publish financial statements and by the increased standard of disclosure required."

From Manuel F. Cohen, "Current Developments at the SEC," The

Accounting Review, January 1965:

In connection with a discussion of the Commission's Special Study, Chairman Cohen went on to state:

"If I may digress for just a moment, I would like to note a rash of similar studies in other countries. In fact, our Special Study may be described as the manifestation in this country of an international trend; a trend which has developed roots in such diverse countries as England, France, West Germany, Canada and several of the emerging nations.

"Similar reforms occurred throughout the western world between 1925 and 1935 when much of the currently existing legislation was formulated here and abroad. The Federal securities laws borrowed the disclosure concept from England. Now, other governments have been advised to look to our practices of providing greater disclosure and control in the distribution and trading of securities. Indeed, commissions appointed in other countries have urged the establishment of regulatory bodies similar to the SEC. The ideas embodied in our laws are proving to be export items.

"Apart from such suggestions, the existing institutions are strengthening their controls very substantially. Thus, accountants and businessmen in England will, like their brethren in this country, soon assume new disclosure responsibilities. As a result of certain corporate failures and takeovers which were accompanied by serious consequences for investors, the London Stock Exchange has recently proposed, and in some cases adopted, new rules calling for greater disclosure of corporate affairs."

From Edward S. Wilson, "The 1964 European Conference Tour,"

Financial Analysts Journal, January - February 1965:

This article describes a European tour by eighty-five security analysts representing constituent societies of The Federation of Financial Analysts in the United States and Canada. With respect to Germany, the statement is made that "Enaction by the government of the Major Company Law by 1966 should lead to the release of substantially more detailed financial information, the first step in developing a more consistent system of analyzing German companies."

The report of the tour concludes with the statement that "it should be emphasized that information being supplied by industrial firms, particularly in West Germany, Holland, and the United Kingdom is much more comprehensive than during our April 1961 trip to Europe."

From David E. Spray, editor, The Principal Stock Exchanges of the

World (1964):

". . . recently it has become customary particularly among the larger and more modern companies [in Italy], to furnish voluntarily more frequent and greater amounts of information regarding the trend of the business" (Chapter Six, "The Stock Markets in Italy," p. 146).

[In England] a "series of Companies Acts, culminating in the Companies Act of 1948, have devised from time to time regulations to afford safeguards and a considerable measure of protection to the prospective investor. Every public invitation to subscribe capital to a company must incorporate in the form of a prospectus a statement of facts which are deemed material to the prospectus of the company and to the security of the capital to be subscribed. While not so extensive as the regulations of the Security and Exchange Commission in the United States, the provisions of the Companies Act of 1948 require the disclosure of all material facts, in the event of knowing non-disclosure or misstatement.

"Furthermore, the Stock Exchange has greatly extended its own control over the quality of securities admitted to quotation. Every prospective new issue is subjected to a searching examination by the Stock Exchange, which takes into account such matters as the adequacy of data furnished, the records of the persons connected with the company, its history, and the arrangements made to secure a free market." (Chapter Eight, "The London Stock Exchange and Other Stock Markets in Great Britain," p. 179).

In Japan, "In order to distribute shares among individual investors and to work for the smooth procurement of funds on the open market, it was imperative that measures be taken for the drastic reform of the securities system and to devise adequate ways to protect the investors. This was the aim of the Securities and Exchange Law of 1948. The Law was patterned after the U. S. Securities Act of 1933, the Securities Exchange Act of 1934, and the Banking Act of 1933. It is the fundamental law governing securities business in Japan." (Chapter Ten, "The Stock Exchanges of Japan," p. 242).

"Although Philippine laws are based on Roman Law and the Code Napoleon, and local institutions developed under the influence of centuries of Spanish domination, financial legislation and institutions in the Philippines are modeled after the American system. The promotion and maintenance of ethical business practices among entrepreneurs, promoters, corporate officers, stockbrokers, security dealers, and investment managers and advisers; the prevention of fraud in security offerings; the assurance of a fair and orderly market for securities; and the protection of investors and stockholders - all these are within the legal and institutional framework of the securities market in the Philippines. (Chapter Eleven, "The Securities Market in The Philippines," p. 285.)