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Corporate and Financial Weekly Digest

APRIL 17, 2009

SEC/CORPORATE

Amendments to Delaware Corporate Law Regarding Shareholder Proxy Access

Effective August 1, the Delaware General Corporation Law will permit a Delaware corporation to adopt a by-law requiring any proxy solicitation materials circulated by the corporation regarding the election of directors to include nominees submitted by stockholders, in addition to those submitted by the corporation. Any such by-law may include minimum ownership requirements as well as a list of other qualifications that a stockholder must comply with in order to nominate a director.

As reported in the March 20, 2009, edition of *Corporate and Financial Weekly Digest*, the Securities and Exchange Commission's current rules permit issuers to exclude stockholder proposals relating to director nominations from their proxy materials. However, SEC Chairman Mary Schapiro has directed the SEC's staff to draft proposals permitting broader stockholder access to issuers' proxy statements for director nominees. It remains to be seen whether the SEC will attempt to preempt state law provisions such as Delaware's.

Other new amendments to Delaware's corporate law (a) permit a Delaware corporation to adopt a by-law requiring corporations to reimburse stockholders for proxy solicitation expenses in connection with director nominations, (b) generally prohibit amendments to a corporation's charter or by-laws that eliminate rights to indemnification or advancement of expenses following an act or occurrence that gives rise to claims for indemnification or advancement, (c) permit Delaware corporations to separate the record date for determining the stockholders entitled to notice of a stockholders' meeting from the record date for determining the stockholders entitled to vote at such meeting, which amendment, at least theoretically, would allow a Delaware corporation to ensure that the economics of ownership of its stock are more closely aligned with voting rights, and (d) allow, in limited circumstances, the judicial removal of a corporation's directors.

New Director of SEC Division of Corporation Finance Named

Securities and Exchange Commission Chairman Mary Schapiro announced this week that Meredith Cross will return to the SEC as Director of the Division of Corporation Finance. Ms. Cross succeeds John White, who resigned several months ago, and Shelly Paratt, who has served as Acting Director in the interim.

While she has been in private practice in Washington, D.C., for the past eleven years, Ms. Cross previously served at the SEC from 1990 through 1998, both as Chief Counsel to, and as Deputy Director of, the Division of Corporation Finance.

Click here to read the SEC's press release.

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Purchases of Condominiums Were Not Investment Contracts Under the Federal Securities Laws

Plaintiffs, customers of defendant StellarOne Bank (StellarOne), brought an action against StellarOne and two individuals, alleging that defendants violated the Securities Act of 1933 and the Securities Exchange Act of 1934 by defrauding them into purchasing condominium units. Plaintiffs claimed that defendants represented that the purchases were "sound investment[s], that no money would actually be required..., that the [plaintiffs] would simply sign a credit application for a non-recourse loan..., that the loans so funded would be used to pay off and prepare the condos for sale, and that [the plaintiffs] would realize a profit on the sale." In reality, plaintiffs signed recourse loans that exceeded the value of the condominiums purchased, virtually guaranteeing that the condominiums would sell for a considerable loss, and leaving plaintiffs personally liable for large deficiency judgments.

Defendants moved to dismiss the claims, arguing, among other things, that the purchases of the condominiums were not securities as defined by the Securities Act and Securities Exchange Act. In response, plaintiffs asserted that because they purchased the condominiums for investment purposes, their purchases were "investment contracts," and therefore included in the definition of securities under the Securities Act and Securities Exchange Act.

The court granted defendants' motion to dismiss, holding that plaintiffs had failed to show that the purchase of the condominiums were "investment contracts." The court pointed out that in interpreting the securities laws, the Supreme Court has defined the term "investment contract" as "a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party." The court ruled that the investments in the condominiums did not fit within this definition because any profits plaintiffs may have derived from the investments would be the result of the potential appreciation in value of the condominiums, which "depended not on the efforts of the [defendants] and the developer, but on the vagaries of the real estate market at the time Plaintiffs attempted to resell their condominiums." (*Inman v. Hall*, No. 7:08cv00567, 2009 WL 960474 (W.D. Va. April 7, 2009))

Third Circuit Reinstates Conviction for Conspiracy to Commit Securities Fraud

Appellee Kevin Heron, Chief Insider Trading Compliance Officer for semiconductor manufacturer Amkor Technology, Inc., was convicted of three counts of securities fraud, as well as one count of conspiracy to commit securities fraud, based on a purported conspiracy with his neighbor, Stephen Sands, a low-level employee of Neoware, to exchange inside information concerning their respective companies. After the jury's verdict convicting Mr. Heron on all counts, the District Court for the Eastern District of Pennsylvania granted his motion for a judgment of acquittal on three of the four counts, including the count of conspiracy to commit securities fraud. The District Court reasoned that a conspiracy to commit securities fraud was a legal impossibility because Mr. Sands, as a low-level employee, was not an insider and therefore not in a position to provide material, non-public information.

After the government appealed, the Third Circuit Court of Appeals reversed and reinstated the conviction. The Third Circuit held that in order to prove conspiracy, the government was required to show that (i) an agreement existed between Mr. Sands and Mr. Heron to exchange and, for trading purposes, use material, non-public information concerning their respective companies, and (ii) at least one overt act in furtherance of that agreement occurred. In reversing the judgment of acquittal on the count of conspiracy to commit securities fraud, the court ruled that whether Mr. Sands was an insider, and therefore legally capable of engaging in securities fraud, was irrelevant to the conspiracy charge. The court reasoned that it is "the conspiratorial agreement itself, not the underlying substantive acts," or the ability to perform them, "that forms the basis for conspiracy charges."

In addition, the Third Circuit ruled that, even if proof of Mr. Sands' insider status was required to prove a conspiracy charge, there was ample evidence from which a jury could have found that he was an insider. The court reasoned that Mr. Sands' position at Neoware was not determinative of his insider status. Instead, the court held, insider status is determined from a person's relationship with the corporation that makes it more probable than not that the individual has access to inside information. In the instant case, the court concluded that there had been sufficient evidence to show that Mr. Sands had access to inside information and agreed to share that information with Mr. Heron. (*U.S. v. Heron*, Nos. 08-1061, 08-1622, 2009 WL 868017 (3rd Cir. April 2, 2009))

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BROKER DEALER

FINRA Filing Makes Changes to Form U4 and U5

The Financial Industry Regulatory Authority made a filing with the Securities and Exchange Commission to amend the Uniform Application for Securities Industry Registration or Transfer (Form U4) and the Uniform Termination Notice for Securities Industry Registration (Form U5). The changes include, among other things, revisions to the arbitration and civil litigation disclosure questions and clarifications to the reporting standards for sales practices violations alleged against registered persons. In addition, the filing raises the monetary threshold for reporting of settlements of customer complaints, arbitrations or civil litigation on the Forms, from $10,000 to $15,000, and revises the definition of "Date of Termination" in Form U5. FINRA indicated that it anticipates including the proposed changes in a software release to the Central Registration Depository at some point in the second quarter of 2009.

To read the filing, click here.

FINRA Adopts Limited Exception to Trade Reporting Rules

The Financial Industry Regulatory Authority issued a Regulatory Notice to announce a filing it made with the Securities and Exchange Commission to adopt a limited exception to its trade reporting rules that will apply to certain transfers of proprietary positions in debt and equity securities between a FINRA member firm and another member firm or non-member broker-dealer. To qualify for the limited exception, the transfer must be effected in connection with a merger of one firm with the other firm or a direct or indirect acquisition of one firm by the other firm or the other firm's parent company, *and* the transfer must not be in furtherance of a trading or investment strategy. The exception applies to the general requirement to report for tape publication purposes; qualifying transfers must continue to be reported to FINRA for regulatory purposes.

Click here to read the FINRA Regulatory Notice.

SEC Approves Three Rules for the Consolidated FINRA Rulebook

In February and March, the Securities and Exchange Commission approved three rules proposed by the Financial Industry Regulatory Authority as part of its process to develop a Consolidated FINRA Rulebook consolidating the different parts of the current FINRA rulebook, which includes the National Association of Securities Dealers (NASD) rules and the rules incorporated from the New York Stock Exchange. Each of the approved rule proposals adopts, with certain modifications, an existing NASD Interpretive Material or NASD Rule as a new consolidated FINRA Rule. These three new consolidated FINRA Rules, which take effect June 15, relate to interfering with the transfer of customer accounts in the context of employment disputes, recommendations to customers in over-the-counter equity securities and anti-intimidation/coordination.

Click here to read FINRA Regulatory Notice discussing the new FINRA Rules.
The SEC releases approving the proposals are available here, here and here.

NASDAQ OMX PHLX Proposes Enhancements to Electronic Trading System

NASDAQ OMX PHLX, Inc. made a rule filing with the Securities and Exchange Commission to implement several enhancements to its current trading system for options, Phlx XL. The enhanced system will be known as Phlx XL II. The proposed changes would impact the system's opening, linkage and routing, quoting, and order management processes.

Click here to read the proposal.

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CFTC

CFTC Adopts Procedures for Confidential Treatment Requests

The Commodity Futures Trading Commission has adopted exclusive procedures for designated contract markets (DCMs), derivatives clearing organizations (DCOs) and derivatives transaction execution facilities (DTEFs) to request confidential treatment for new products and new rules and rule amendments submitted to the CFTC. The specific requirements appear in CFTC Regulation 40.8, and require that requests for confidential treatment of new product submissions, rules or rule amendments filed with the CFTC for review and approval or submitted pursuant to the CFTC's self-certification process be filed under cover of a request for confidential treatment. The request must set out a detailed written justification for the request (in the form and with the content required by CFTC Regulation 145.9), with the material for which confidential treatment is being requested being segregated in an appendix to the submission. Submissions not filed under cover of a request for confidential treatment will be treated as public information.

The new procedures will become effective on May 15.

Click here to read the Federal Register release announcing the adoption of these rules.

CFTC Approves New NFA Rules Regarding Forex Orders

The Commodity Futures Trading Commission has approved new National Futures Association (NFA) Compliance Rule 2-43, relating to adjustments to customer forex orders and the offset of customer forex positions by forex dealer members (FDMs). NFA Compliance Rule 2-43(a) prohibits FDMs from adjusting the price of executed customer orders except where (i) the adjustment is favorable to the customer and is made to settle a customer complaint, or (ii) the FDM exclusively operates a "straight-through processing" platform and the counterparty cancels or adjusts the price. In the latter case, the FDM is required to provide written notice to the customer within 15 minutes of execution and either cancel the order(s) or adjust the accounts of all similarly situated customers, as provided in the Rule.

NFA Compliance Rule 2-43(b) separately prohibits FDMs from allowing customers to carry offsetting positions and generally requires an FDM to offset positions in a customer account on a first-in, first-out basis. The Rule permits the FDM to offset same-size transactions at the customer's request, however, even if there are older transactions of a different size in the account (provided that the offset must be against the oldest same-size transaction). Rule 2-43(a) will become effective as to all customer orders executed after June 12; Rule 2-43(b) will become effective for positions established after May 15.

Click here to read the NFA Notice to Members announcing the new Rules.

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BANKING

OTS Issues Mortgage Scam Alert

On April 14, the Office of Thrift Supervision (OTS) issued an alert to consumers with advice regarding the avoidance of foreclosure rescue scams typically undertaken by companies or individuals who refer to themselves as "foreclosure consultants" or "foreclosure specialists". The alert, entitled *Foreclosure Rescue Scams: How to Avoid Becoming A Victim*, notes that this type of fraud is increasing as U.S. foreclosure rates increase.

According to the OTS' release, three types of scams are common: (i) phantom help – the purported company or individual charges high fees for no work or for services the homeowner could have undertaken on his own; (ii) bailout – a homeowner surrenders his title to the home after receiving false assurance that he can remain as a renter and buy back the property later; and (iii) bait and switch – consumers are told they can refinance their homes

but instead sign documents that transfer title of their properties to scam companies while the consumers remain responsible for the mortgage payments.

For more information, click here.

TARP Capital Purchase Program Expanded to Include Mutual Holding Companies

For a Katten *Client Advisory* on the topic, click here.

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STRUCTURED FINANCE AND SECURITIZATION

FRBNY Responds to Congressional Oversight Panel Inquiry and Promises to Release Guidance on TALF Investment Funds

On April 7, the Federal Reserve Bank of New York (FRBNY) published a letter dated April 1 from both the FRBNY and the Board of Governors of the Federal Reserve System to Elizabeth Warren, the Chair of the Troubled Asset Relief Program Congressional Oversight Panel (COP). The letter was sent in response to a March 20 inquiry by the COP regarding the FRBNY's Term Asset-Backed Securities Lending Facility (TALF). In its inquiry, the COP posed a number of questions and raised criticisms regarding the TALF program, and specifically referred to a March 14 article in the Wall Street Journal titled "TALF Is Reworked After Investors Balk", in which it was reported that "Wall Street dealers... have created vehicles to participate in the TALF that would allow investors in the program to circumvent many of the restrictions laid out by the Fed. The vehicles resemble collateralized debt obligations, or CDOs, and use some of the financial engineering that was partially responsible for the collapse of the credit markets."

In its response, the FRBNY stated that "[t]he Wall Street Journal provided an inaccurate portrayal of our position with respect to the reported proposals of certain dealers as they regard 'vehicles [created] to participate in TALF that would allow investors in the program to circumvent many of the restrictions laid out by the Fed.' The Federal Reserve expects to release guidance shortly that will clarify the legal and compliance standards applicable to investment funds, with the aim of ensuring that all borrowers in the program, regardless of investor type, meet a common set of eligibility standards. The guidance will be published on our website."

Click here to read the FRBNY response letter.

IRS Issues REMIC Guidance on Home Affordable Modification Program

On April 10, the Internal Revenue Service released new guidance assisting servicers of residential loan pools taking advantage of the Treasury Department's Home Affordable Modification Program. First, the IRS released Rev. Proc. 2009-23, assuring that modifications to residential mortgage loans pursuant to the program will not cause disqualification of any real estate mortgage investment conduit (REMIC) or grantor trust. Second, the IRS released Notice 2009-36, stating that pursuant to the Notice and new regulations, any incentive or other payment made to a REMIC under the program will not be subject to the 100% tax on prohibited contributions to a REMIC.

Read Rev. Proc. 2009-23 and Notice 2009-36.

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