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CORPORATE & FINANCIAL
WEEKLY DIGEST

August 17, 2012

SEC/CORPORATE

New Disclosure Requirements Imposed in Connection with Iran Sanctions

On August 10, President Obama signed into law the Iran Threat Reduction and Syria Human Rights Act of 2012 (the Act), which expands and establishes additional sanctions with respect to Iran, including sanctions relating to energy, development of weapons of mass destruction, certain activities of financial institutions, and human rights abuses. In addition to an increase in sanctions, the Act includes new mandatory disclosure requirements under the Securities Exchange Act of 1934 (the Exchange Act).

The Act amends the Exchange Act to require issuers that are required to file annual or quarterly reports under Section 13 to make additional disclosures with respect to certain activities relating to Iran. Issuers must disclose whether, during the period covered by the report, they or any of their affiliates knowingly:

- engaged in activities described in Sections 5(a) or 5(b) of the Iran Sanctions Act of 1996 (including certain investments or the provision of goods or services that contribute to Iran's ability to develop petroleum resources or acquire or develop weapons of mass destruction);
- engaged in activities described in Sections 104(c)(2), 104(d)(1) or 105A(b)(2) of the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 (including certain activities by foreign financial institutions that facilitate the efforts of the government of Iran or certain other persons relating to terrorism and weapons of mass destruction and transactions by persons owned or controlled by a domestic financial institution that benefit certain Iranian governmental entities);
- conducted any transaction or dealing with certain persons who are blocked pursuant to certain executive orders; or
- conducted any transaction or dealing with certain persons related to the government of Iran without authorization from a federal department or agency.

An issuer disclosing any of the above information must include a detailed description of each activity, including the nature and extent of the activity, the gross revenues and net profits attributable to the activity and whether the issuer or its affiliate intends to continue the activity.

Issuers reporting such information will also be required to separately file with the Securities and Exchange Commission a notice that the disclosure was made. The SEC will then transmit the report containing the disclosure to the President and Congress and will make the information available on the internet. Upon receiving such a report from the SEC, the President must initiate an investigation regarding possible sanctions that may be imposed.

This amendment to Section 13 of the Exchange Act is effective for quarterly and annual reports required to be filed with the SEC after February 6, 2013.

To view the full text of the Act, click here.

CFTC

CFTC Proposes Inter-Affiliate Clearing Exemption

On August 16, the Commodity Futures Trading Commission issued a proposed rule to exempt swaps between certain affiliated entities from the clearing requirement set forth in the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act). The Dodd-Frank Act amended the Commodity Exchange Act to establish a clearing requirement, which makes it unlawful for any person to engage in a swap that is subject to the mandatory clearing requirement unless that swap is submitted to a derivatives clearing organization.

Under the proposed rule, counterparties may elect not to clear a swap if one counterparty directly or indirectly holds a majority ownership interest in the other or a third party directly or indirectly holds a majority ownership interest in both counterparties and the financial statements of both counterparties are reported on a consolidated basis. Eligible counterparties must also satisfy the following conditions: (i) both counterparties must elect not to clear the swap; (ii) the swap trading relationship must be adequately documented; (iii) a centralized risk management program must be used to monitor and manage the risks of the swap; (iv) variation margin must be collected unless there is 100% common ownership of the counterparties; (v) the swap reporting requirements must be fulfilled; and (vi) both counterparties must be located in the United States or, if not, the foreign affiliate must be located in a jurisdiction that has a comparable and comprehensive clearing requirement, be required to clear swaps with non-affiliated counterparties under US law, or not enter into swaps with non-affiliated parties.

Commissioners Sommers and O'Malia dissented. The dissenting Commissioners support a clearing exemption for swaps between affiliated entities within a corporate group, but did not support the proposed rule to the extent it requires variation margin to be paid by corporate entities that engage in inter-affiliate trades.

The proposed rule is available here.

CFTC Issues Temporary No-Action Relief for Trade Options

On August 14, the Commodity Future Trading Commission's Division of Market Oversight (DMO) granted market participants temporary no-action relief from certain regulatory requirements for trade options, as defined in CFTC Regulation 32.3(a). On April 27, the Commission published final rules for commodity options, which included an interim final rule that applies to trade options. This interim final rule specified that trade options would be subject to certain CFTC regulations, including swap data recordkeeping requirements, large trader reporting, position limits, duties of swap dealers (SDs) and major swap participants (MSPs), reporting and recordkeeping requirements for SDs and MSPs, capital and margin requirements for SDs and MSPs, and the prohibition against fraud, manipulation and other abusive practices and related enforcement provisions.

The Division of Market Oversight's no-action letter grants relief for trade options from all of the regulatory requirements listed above, except for those related to position limits, the prohibitions of fraud, manipulation and other abusive practices, and related enforcement provisions. The no-action relief will remain in effect until the earlier of: (i) December 31, 2012; or (ii) the effective date of a final trade option rule or interpretive order issued by the CFTC.

The no-action letter is available here.

CFTC Issues Guidance on Compliance Obligations for CPOs and CTAs

On August 14, the Commodity Futures Trading Commission issued a set of responses to frequently asked questions (FAQs) related to the compliance obligations of commodity pool operators (CPOs) and commodity trading advisors. The FAQs address a variety of issues and concerns that have been raised by market participants, including compliance dates, wholly owned subsidiaries, trading limits, the CPO registration exemption conferred by CFTC Regulation 4.13(a)(3), and the process for transitioning from a registration exemption under now-repealed Regulation 4.13(a)(4) to CPO registration or another exemption from registration. The FAQs indicate, for example, that the CPO of a pool that was previously exempt under Regulation 4.13(a)(4) may claim disclosure, reporting and recordkeeping relief under Regulation 4.7 even though the pool did not file the notice required under Regulation 4.7(d) as long as interests in the pool were offered and sold in a manner that was consistent with the then-effective provisions of Part 4.

The FAQs are available here.

LITIGATION

New York Court Adopts Delaware Test for Determining Direct and Derivative Claims

The New York Appellate Division recently adopted the Delaware test for determining whether a plaintiff's claims are direct or derivative in nature.

Plaintiffs, trustees of a member of a joint venture that owned and managed a shopping center, sued other members of the joint venture and the managing agent of the shopping center, alleging mismanagement of the shopping center's property and finances. Plaintiffs purported to assert both derivative and direct claims, including waste, breach of contract, breach of fiduciary duty, and negligence claims. The lower court dismissed Plaintiffs' claims, holding that the claims were entirely derivative in nature, and that Plaintiffs had failed to plead demand futility, which is required to successfully plead derivative claims.

Plaintiffs appealed, asserting that some of their claims were direct in nature and therefore did not require allegations of demand futility. After finding that New York courts do not have a uniform test for determining if a claim is direct or derivative in nature, the Appellate Division adopted the standard established in the Delaware courts. The Delaware standard holds that a direct claim must allege an injury to a plaintiff that is "independent of any alleged injury to the corporation" in which the plaintiff holds a financial interest. In addition, a plaintiff bringing a direct claim "must demonstrate that the duty breached was owed to [plaintiff] and that he or she can prevail without showing an injury to the corporation." The Appellate Division held that all of Plaintiffs' claims were based on alleged injuries to the joint venture that controlled the shopping center. Accordingly, Plaintiffs were required to plead demand futility for all of their claims. Because Plaintiffs failed to do so, the Appellate Division upheld the lower court's dismissal of all of Plaintiffs' claims.

Yudell v. Gilbert, --- N.Y.S.2d ----, 2012 N.Y. Slip Op. 05896, 2012 WL 3166788 (1st Dept. Aug. 7, 2012).

Second Circuit Addresses Standard for SEC Aider and Abettor Actions

The US Court of Appeals for the Second Circuit recently held that when the Securities and Exchange Commission brings an enforcement action against a defendant that has allegedly aided and abetted a securities law violation, the SEC is not required to plead that the defendant has proximately caused the injury resulting from the violation.

The SEC charged defendant, the chief financial officer of an equipment manufacturer, with aiding and abetting a fraudulent accounting scheme that violated federal securities laws. In order to bring an enforcement action against a defendant for aiding and abetting a securities violation, the SEC must adequately plead: (1) the existence of securities law violation by the primary party; (2) defendant's knowledge of the violation; and (3) "substantial assistance" by the defendant in the achievement of the violation. The District Court held that for the SEC to adequately plead that the defendant had "substantially assisted" in a securities violation, the SEC must plead that the defendant had proximately caused the injury that resulted from the alleged securities violation. The District Court found that the SEC had not adequately pleaded proximate causation and dismissed the complaint. The SEC appealed the dismissal to the Second Circuit.

The Court of Appeals reversed. It found that the SEC could successfully plead that an aider and abettor defendant had "substantially assisted" in the achievement of a securities violation without pleading that the defendant had proximately caused an injury that resulted from the violation. The Court reasoned that because SEC enforcement actions against aiders and abettors were to deter future securities violation, as opposed to direct compensation for the injury resulting from the violation, proximate causation of the injury was not a required component of liability.

The Court of Appeals reexamined the SEC's allegations against defendant and found that the SEC had sufficiently pleaded all of the elements of aider and abettor liability, including "substantial assistance." Accordingly, the Court of Appeals reversed the District Court's grant of defendant's motion to dismiss.

SEC v. Apuzzo, No. 11–696–cv, 2012 WL 3194303 (2d Cir. August 8, 2012).

UK DEVELOPMENTS

LIBOR Review Discussion Paper Published

On August 10, HM Treasury published an initial discussion paper of the LIBOR Review which is being conducted by Martin Wheatley, the CEO-designate of the Financial Conduct Authority. The Review is charged with reporting on:

- necessary reforms to the current framework for setting and governing LIBOR;
- the adequacy and scope of sanctions to appropriately tackle LIBOR abuse; and
- whether analysis of the failings of LIBOR has implications on other global benchmarks.

The discussion paper sets out the Review's initial view on the issues to be considered. It states that LIBOR has a number of significant weaknesses that have eroded its credibility as a benchmark and that retaining LIBOR unchanged in its current state is not a viable option, given the scale of identified weaknesses and the loss of credibility that it has suffered. LIBOR has to be significantly strengthened to take account of these weaknesses, while alternative benchmarks that can take on some or all of the roles that LIBOR currently performs in the market should be identified and evaluated.

The discussion paper sets out detailed ideas on how LIBOR could be comprehensively reformed and strengthened. It also observes that the issues that have been identified with LIBOR have broader implications for a range of other benchmarks, both within financial markets and beyond. It suggests that it is worth considering whether it is possible to establish a clear set of principles or characteristics that should be applied to all globally used benchmarks. These could include:

- a robust methodology for calculation;
- credible governance structures;
- an appropriate degree of formal oversight and regulation; and
- transparency and openness.

The LIBOR Review consultation period lasts only until September 7 as it is aiming to present its findings to the Chancellor of the Exchequer before the end of September.

For more information, click here.

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