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CORPORATE & FINANCIAL
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SEC/CORPORATE

NYSE Proposes Tougher Listing Standards for Issuers Following Reverse Mergers

On August 4, the New York Stock Exchange LLC filed a proposed rule change with the Securities and Exchange Commission to adopt additional initial listing requirements for companies that have become public through transactions in which unlisted private operating companies merge into publicly traded shell companies, commonly known as reverse mergers. The proposed amendments are similar to rules proposed by the NASDAQ Stock Market LLC and described in the April 29 edition of the *Corporate and Financial Weekly Digest*.

According to the NYSE, the amendments to Rules 102.01 and 103.01 are being proposed in response to widespread concerns of accounting fraud by reverse merger companies. The proposed amendments provide that a reverse merger company would not be eligible for listing unless the combined entity had immediate preceding the filing of its initial listing application:

- traded for at least one year in the U.S. over-the-counter market, on another national securities exchange or on a regulated foreign exchange following the consummation of the reverse merger and (a) in the case of a domestic issuer, filed with the SEC a Form 8-K including all of the information required under Item 2.01 of Form 8-K, including all required audited financial statements, or (b) in the case of a foreign private issuer, filed the information described in (a) above on Form 20-F;

- maintained a minimum stock price of at least $4 on both an absolute and an average basis for a sustained period; and

- timely filed with the SEC all required reports since the consummation of the reverse merger, including the filing of at least one annual report containing audited financial statements for a full fiscal year commencing on a date after the date of the filing described in the first bullet point above.

Additionally, a reverse merger company would be required to maintain on an absolute and average basis a minimum stock price of at least $4 through listing. The NYSE's definition of reverse merger would exclude the acquisition of an operating company by a listed company that qualified for listing as a Special Purpose Acquisition Company (SPAC). The NYSE would also exclude reverse merger transactions if the listing was in connection with an initial firm commitment underwritten public offering where the proceeds to the reverse merger company were sufficient to generate $40 million in aggregate market value of publicly-held shares and the offering was occurring subsequent to or concurrently with the reverse merger.

To read the rule change, click here.

SEC's New Whistleblower Rules in Effect

On August 12, the Securities and Exchange Commission's new whistleblower rules went into effect. The whistleblower rules were described in the May 27 edition of the *Corporate and Financial Weekly Digest.* In addition, the SEC activated a new "Office of the Whistleblower" web page for submission of tips and to provide other information on the whistleblower rules.

To view the whistleblower web page, click here.

BROKER DEALER

SEC Temporarily Exempts Floor Brokers Handling Orders Manually from the Automated Controls Requirement of Rule 15c3-5

On August 15, the Securities and Exchange Commission released an order "temporarily exempting the floor broker operations of broker-dealers with market access that handle orders on a manual basis" (the Floor Brokers) from the automated controls requirement of Rules 15c3-5(c)(1)(ii) and (c)(2) of the Securities Exchange Act of 1934 (the Automated Controls Rule). The Automated Controls Rule applies to each broker-dealer with market access to an exchange or automated trading system and requires, among other things, that each such broker-dealer implement a risk management control system and supervisory procedures reasonably designed to:

- systematically limit the broker-dealer's financial exposure due to market access and ensure compliance with regulatory requirements in respect of market access;

- prevent entry of orders that exceed pre-set capital or credit thresholds, appear to be erroneous or such broker-dealer or customer is prohibited from trading and ensure compliance with all other pre-entry regulatory requirements; and

- restrict market access technology systems to authorized persons and ensure appropriate surveillance personnel receive immediate post-trade execution reports.

The SEC has extended the date for compliance with the Automated Controls Rule for Floor Brokers until November 30. Since the Floor Brokers have historically controlled the risks noted above on a manual basis, the SEC was willing to grant such Floor Brokers additional time to complete the development and implementation of automated controls for such manual orders.

To read SEC Release No. 34-65132, click here.

CFTC

CFTC Approves Amendments to NFA Forex Requirements

The Commodity Futures Trading Commission has approved proposed amendments to National Futures Association compliance rules, bylaws and other requirements applicable to the retail forex activities of NFA members.

Among the amendments, NFA is eliminating certain existing exclusions from compliance with NFA's forex requirements, with the result that all NFA members engaging in retail forex transactions will be subject to the applicable NFA forex requirements (subject to a limited exemption for futures commission merchants (FCMs) whose forex activities are limited to hedging currency risk for their futures customers). Currently, NFA's retail forex requirements do not apply to FCMs and introducing brokers that are also registered with the Securities and Exchange Commission as broker-dealers.

NFA is also amending its bylaws to require that (i) any NFA member that is registered with the CFTC and conducting forex activities be designated as a forex firm and (ii) any individual associated with such a firm be approved as a forex associate in order to conduct forex activities for the firm. Such firms must have at least one principal registered as an associated person (AP) and approved as a forex AP.

The amendments also apply the “know-your-customer” requirements set forth in Compliance Rule 2-30 to NFA members’ forex transactions, and require NFA forex dealer members (FDMs) to maintain an office within the United States (including Puerto Rico) that is responsible for preparing and maintaining CFTC- and NFA-required financial records and reports (which such office must be under the supervision of a listed principal and registered AP of the FDM residing in that office).

The amendments will take effect on October 1. To read a copy of NFA’s release, click here.

LITIGATION

Second Circuit Affirms Madoff Trustee’s Net Equity Calculation

The United States Court of Appeals for the Second Circuit found in favor of the trustee (the Trustee) presiding over the liquidation of Bernard L. Madoff Investment Securities (BMIS), affirming the Trustee’s calculation of “net equity” in the BMIS liquidation. The Trustee calculates net equity to determine the value of claims submitted by victims of Madoff’s massive fraud.

The dispute focused on two methods for calculating net equity. The Trustee argued that net equity should be based on the ‘Net Investment Method,’ which credited the amount of cash deposited by the customer into his or her BMIS account, less amounts withdrawn. The customers objecting to the Trustee’s proposed method advocated the so-called ‘Last Statement Method,’ which would calculate net equity based on the market value of securities reflected on their last BMIS customer statements. After reviewing the relevant statutory provisions, the Second Circuit ruled in favor of the Trustee and the Net Investment Method, holding that the last statements, produced by Madoff and his fraudulent enterprise were totally unreliable, and that “if the Trustee had permitted the objecting claimants to recover based on their final account statements, this would have ‘affected the limited amount available for distribution from the customer property fund’ . . . . The inequitable consequence of such a scheme would be that those who had already withdrawn cash deriving from imaginary profits in excess of their initial investment would derive additional benefit at the expense of those customers who had not withdrawn funds before the fraud was exposed.” In so ruling, the court was careful to say that the Net Equity Method was not the only way for a Securities Investor Protection Act trustee to calculate net equity, and that the facts and circumstances of particular cases could oftentimes require a different method to be used.

In re Bernard L. Madoff Investment Securities LLC, 10-2378 (2d Cir. August 16, 2011).

Court Finds Arbitration Clauses Cell Phone Contracts do not Apply to Collection Agency

Customers who had signed cell phone contracts with Verizon and AT&T, brought a class action against the collection agency that the phone companies hired to collect unpaid fees and charges. The complaint alleged that the agency, Collecto, Inc., violated the Fair Debt Collection Practices Act and New York’s consumer protection statute and committed common law fraud by seeking payment of collection costs in addition to the unpaid fees owed to phone companies. Collecto moved to compel the plaintiffs to arbitrate their claims, arguing that the mandatory arbitration clauses in the agreements between the plaintiffs and the phone companies should also apply to Collecto.

The U.S. District Court for the Southern District of New York acknowledged the strong public policy favoring arbitration, but held that the arbitration clauses in the customer contracts did not apply to Collecto. Although the agreements between the plaintiffs and the phone companies did not mention Collecto, Collecto argued that it should be considered the phone companies’ agent when it collected fees in connection with the plaintiffs’ agreements. The court found insufficient evidence to support Collecto’s claim that it had an agency relationship with the phone companies. To the contrary, the court pointed to Collecto’s contracts with Verizon and AT&T, which expressly designated Collecto as an independent contractor, as opposed to an agent. Consequently, the court declined to compel the plaintiffs’ to arbitrate their claims against Collecto.

Butto, et. al. v. Collecto, Inc., No. 10-CV-2906 (ADS)(AKT), 2011 WL 3557310 (E.D.N.Y. August 15, 2011).

BANKING

Federal Reserve Issues Interim Rules for Savings and Loan Holding Companies

The Federal Reserve (the Board) on August 12 issued an interim final rule establishing regulations for savings and loan holding companies (SLHCs). Under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act), supervisory and rulemaking authority for SLHCs and their nondepository subsidiaries transferred from the Office of Thrift Supervision (OTS) (now defunct) to the Board on July 21, 2011. Last month, the Federal Reserve sought comment on a notice identifying regulations previously issued by the OTS that the Federal Reserve will continue to enforce. The interim final rule issued on August 12 implements the transfer of those regulations from the OTS to the Federal Reserve.

The interim final rule has three components: (1) new Regulation LL (Part 238), which sets forth regulations generally governing SLHCs; (2) new Regulation MM (Part 239), which sets forth regulations governing SLHCs in mutual form; and (3) technical amendments to current Board regulations necessary to accommodate the transfer of supervisory authority for SLHCs from the OTS to the Board.

In drafting new Regulation LL, the Board has sought to collect all current OTS regulations applicable to SLHCs (other than regulations pertaining uniquely to SLHCs in mutual form) and transfer them into a single part of Chapter 2 of Title 12 for ease of locating. Generally, the structure of the new Regulation LL closely follows that of the Board's Regulation Y, which houses regulations directly related to bank holding companies (BHCs), in order to provide an overall structure to rules that were previously found in disparate locations. In many instances, this process has involved copying the current OTS regulations into the new Regulation LL with only technical modifications to account for the shift in supervisory responsibility from the OTS to the Board. The Board also made several substantive changes to the OTS regulations as they were incorporated into Regulation LL. Additionally, the Board added or modified regulations to reflect substantive changes introduced by the Dodd-Frank Act. The modifications relate to application processing, control determinations, financial holding company activities, activities 'closely related to banking,' insurance agency activities, certain grandfathered activities, and the declaration of dividends by subsidiary savings associations.

Regulation MM organizes the current OTS regulations specific to SLHCs in mutual form (MHCs) and their subsidiary holding companies into a single part of the Board's regulations. Previously, regulations governing MHCs were largely found in parts 575 and 563b of the OTS rules. In many cases, Regulation MM mirrors the current OTS rules with only technical modifications to account for the shift in supervisory responsibility from the OTS to the Board. Regulation MM also reflects several substantive changes to OTS regulations.

Finally, technical amendments were made to current Board regulations necessary to accommodate the transfer of supervisory authority for SLHCs from the OTS to the Board.

The Board on August 12 also issued an Order delegating to staff and to the Reserve Banks the authority to take certain actions with respect to SLHCs.

The Board will accept comments on the interim final rule through October 27.

For more information about the interim rule, click here and here.

EXECUTIVE COMPENSATION AND ERISA

HHS Issues Proposed Rule for Employer Participation in State Heath Care Exchanges

Pursuant to the Patient Protection and Affordable Care Act, beginning in 2014 individuals and small businesses will have access to the purchase of private health insurance through insurance exchanges. States are required to set up health insurance exchange markets, both for small businesses (the Small Business Health Option Program, or SHOP) and for individuals, or a single exchange that combines both. Forty-nine states have applied for grants to help plan and operate exchanges.

On August 12, the United States Department of Health and Human Services released a proposed rule titled the 'Exchange Eligibility and Employer Standards,' which attempts to create uniform standards and systems for enrolling in insurance plans through the exchanges. The goal is to provide 'competitive marketplaces for individuals and small employers to directly compare available private health insurance options on the basis of price, quality, and other factors.'

The proposed rule tackles the issue of eligibility for both exchange participation and insurance affordability programs by proposing a coordinated electronic system that will verify income and eligibility almost instantaneously. This will be accomplished by use of data matching with electronic data sources. Furthermore, the proposed rule streamlines the eligibility rules for tax credits, Medicaid, and Children's Health Insurance Program to enable the consumer to enroll in the proper program without duplicative steps or paperwork among the different programs. The key goal of the proposed rule is to allow many, if not most, individuals to receive an eligibility determination and enroll in a health plan in one session. After enrollment, the proposed rule also creates policies and procedures for a redetermination process to ensure that only qualified enrollees remain eligible for participation in the exchange and any affordability programs.

The rule also contains standards for employers participating in SHOP, which focus mainly on ensuring employers that are participating are eligible to do so, and ensuring their dissemination of information and availability of the exchanges to their employees.

The rule was published in the Federal Register on August 17, and can be accessed here. There will be a period of 75 days for public comment.

EU DEVELOPMENTS

European Regulators Impose Short Sale Bans

On August 11, the financial regulators in Belgium, France, Italy and Spain introduced short selling restrictions on shares of certain named financial institutions and derivatives (e.g., futures) linked to those securities. The restrictions also extend to stock indices of which those securities are components.

The Belgian restrictions apply indefinitely. The three other countries' restrictions will expire after 15 days, unless extended. Earlier that week, Greece imposed a two-month ban on short sales of all listed securities.

The regulators' interpretations of their restrictions are constantly evolving. Changes generally are reflected in amendments to published FAQs. The websites below should be consulted for the most up to date information.

Belgium
To read the announcement click here.
To review FAQs click here.
To visit the FSMA website click here.

France
To read the announcement click here.
To review FAQs click here.
To visit the AMF website click here.

Italy
To read the announcement click here.
To review FAQs click here.
To visit the CONSOB website click here.

Spain
To read the announcement click here.
To visit the CNMV website click here.

Greece
To read the announcement click here.
For further guidance click here.
To visit the HCMC website click here.

ESMA Issues Statement on Short Selling and Market Abuse

On August 11, in the context of the short selling restrictions introduced by Belgium, France, Italy and Spain, the European Securities and Markets Authority (ESMA) issued a statement reiterating the requirements set out in the European Union Market Abuse Directive (MAD) and implemented in national laws that prohibit the dissemination of information which gives, or is likely to give, false or misleading signals as to financial instruments. This clearly includes the dissemination of rumors and false or misleading information.

ESMA emphasized that European financial regulators will take a firm stance against any behavior that breaches these requirements and ESMA will give the national authorities its full support. ESMA pointed out that while short-selling can be a valid trading strategy, when used in combination with spreading false market rumors is clearly abusive.

ESMA also pointed out that the short selling restrictions introduced by Belgium, France, Italy and Spain "have been aligned as far as possible in the absence of a common EU legal framework in the area of short-selling and given the very different national legal bases on which such measures can be taken."

To read the statement made by ESMA, click here.

UK DEVELOPMENTS

Fund Manager CEO and CFO Fined and Banned for Misleading Investors and Market Abuse

The Upper Tribunal (Tax and Chancery Chamber) has published its decision in *Michiel Visser and Oluwole Fagbulu v. FSA*.

Michiel Visser and Oluwole Fagbulu were fined respectively £2 million (approximately $3.3 million) and £500,000 (approximately $830,000). The fine on Fagbulu was reduced to £100,000 (approximately $166,000) on the grounds of financial hardship. Visser was CEO and Fagbulu CFO of Mercurius Capital Management Ltd (Mercurius), a UK FSA authorized entity that managed Mercurius International Fund Ltd (the Fund), a Cayman Islands hedge fund. During the relevant period from July 2006 to January 2008, the Fund had about 20 investors who had collectively invested approximately EUR 35 million (approximately $50 million). The Fund was placed in voluntary liquidation on January 11, 2008.

The Tribunal upheld the FSA's findings that Visser and Fagbulu:

- committed market abuse in the form of market manipulation to bolster the Fund's net asset value;
- repeatedly disregarded the investment restrictions set out in the Fund's offering memorandum;
- undertook fictitious transactions designed to give an inflated and false impression of the value of the Fund's assets; and
- repeatedly issued misleading communications to investors.

The fines were imposed for breach of Principle 1 of the FSA's statements of principle for approved persons (APER), which requires an approved person to act with integrity, and for market abuse. Both men were also banned from performing any regulated activity in the future.

The Tribunal accepted that Fagbulu may not have fully understood the nature of his actions. This was not a defense nor an excuse. As the designated compliance officer, he failed to perform his duty to ensure that Mercurius complied with the relevant regulatory requirements.

The fine imposed on Visser is the largest ever imposed on an individual by the FSA.

Tracey McDermott, acting director of enforcement and financial crime, said:

> "Visser and Fagbulu's conduct fell woefully short of the standards required of approved persons. They showed a flagrant disregard for the interests of their investors and over a considerable period engaged in a sustained and deliberate course of deception to present a picture of the fund's performance that was entirely false.
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> "The Tribunal described Visser's conduct as the worst it had seen. We welcome the significant penalties imposed by the Tribunal in this case and its reiteration of the fundamental principles underpinning the regulatory regime – that approved persons must take responsibility for their conduct, that bans must be imposed where misconduct such as this is identified in order to protect the public and that penalties must both register disapproval of the individuals' misconduct and be sufficient to deter others from similar actions."

To read the decision, click here.

Former Chairman of Wm Morrison Supermarkets Plc Fined for Breach of Share Disclosure Rules

On August 16, the UK Financial Services Authority (FSA) announced that it had published a final notice imposing a penalty of £210,000 (approximately $350,000) on Sir Ken Morrison (KM), the former chairman of Wm Morrison Supermarkets Plc, for breach of its shareholding disclosure rule DTR 5.8.3R.

Between September 16, 2009, and June 21, 2010, KM's voting rights in Wm Morrison Supermarkets Plc had fallen below the 6%, 5%, 4% and 3% thresholds under which notification was required. KM failed to notify the company of the reductions in his voting rights until March 1, 2011. The result of this failure was that the company was not in a position to provide the required information to the market in accordance with DTR 5.8.12R(1) and consequently the market was misled as to the ownership of voting rights in the company. In addition, KM's shareholding was consequently misstated in the company's January 2010 annual report.

KM explained his failure to make the required notifications by claiming he was unaware of the disclosure requirements.

The FSA considered the failings serious, due to KM's prominent position and significant delay in his eventually making the required notification.

KM agreed to settle at an early stage of the FSA's investigation and so qualified for a 30% reduction of the financial penalty. The FSA decided to impose a total financial penalty of £210,000 (approximately $350,000), but for the early settlement discount the FSA would have imposed a fine of £300,000 (approximately $500,000).

Tracey McDermott, acting director of enforcement and financial crime, said:

> "It is important that significant shareholders recognize that timely and accurate disclosure of their shareholdings and voting rights is a fundamental component of a properly informed securities market. Investors are entitled to know when major and influential shareholders significantly reduce their interest in a listed company. Sir Ken should have been aware of his obligations and his failure to meet them has resulted in this fine.
>
> "The rules are designed to enhance transparency and provide investors with timely information regarding voting rights in issuers. Failure to comply with the rules risks damaging investor confidence in the financial markets."

To read the FSA's announcement, click here.

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