Katten
Katten Muchin Rosenman LLP

Corporate and Financial Weekly Digest

January 9, 2009

SEC/Corporate

SEC Releases Congressionally Mandated Report on Fair Value Accounting Standards

On December 30, 2008, the Securities and Exchange Commission delivered a report to Congress mandated by the Emergency Economic Stabilization Act of 2008 (EESA) recommending improving fair value accounting standards rather than suspending them. The report, titled *Report and Recommendations Pursuant to Section 133 of the Emergency Economic Stabilization Act of 2008 (EESA): Study on Mark-To-Market Accounting*, by the SEC's Office of the Chief Accountant and Division of Corporation Finance, recommends improvements to existing practice, including reconsidering the accounting for impairments and the development of additional guidance for determining fair value of investments in inactive markets, including situations where market prices are not readily available.

The EESA mandated that the SEC, the Board of Governors of the Federal Reserve System and the Secretary of the Treasury conduct a study on mark-to-market accounting standards as provided by Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* (SFAS No.157). Other accounting standards in various ways require what is more broadly known as "fair value" accounting, of which mark-to-market accounting is a subset. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in U.S. GAAP and requires expanded disclosures about fair value measurements.

The report addresses the following six key issues:

- The effects of such accounting standards on a financial institution's balance sheet
- The impacts of such accounting on bank failures in 2008 (The report stated that fair value accounting did not appear to play a meaningful role in the bank failures that occurred in 2008)
- The impact of such standards on the quality of financial information available to investors
- The process used by the FASB in developing accounting standards
- The advisability and feasibility of modifications to such standards
- Alternative accounting standards to those provided in SFAS No. 157

The report outlined the following recommendations:

- SFAS No. 157 should be improved, not suspended.
- Existing fair value and mark-to-market requirements should not be suspended.
- While fair value standards should not be suspended, additional measures should be taken to improve the application and practice related to existing fair value requirements.

SEC/CORPORATE

For more information, contact:

Robert L. Kohl
212.940.6380
robert.kohl@kattenlaw.com

Mark A. Conley
310.788.4690
mark.conley@kattenlaw.com

Palash I. Pandya
212.940.6451
palash.pandya@kattenlaw.com

- In determining how to address the above issues, the FASB should consider which issues could be resolved through a review of the objectives of SFAS No. 157 and which issues would be best addressed by the valuation community.
- The accounting for financial asset impairments should be readdressed.
- Implement further guidance to foster the use of sound judgment.
- Accounting standards should continue to be established to meet the need of investors.
- Additional formal measures to address the operation of existing accounting standards in practice should be established.
- Address the need to simplify the accounting for investments in financial assets.

The report also recommends that the FASB reassess current impairment accounting models for financial instruments, including consideration of narrowing the number of models under U.S. GAAP.

http://www.sec.gov/news/press/2008/2008-307.htm
http://www.sec.gov/news/studies/2008/marktomarket123008.pdf

Shelley Parratt Named Acting Director of SEC's Division of Corporation Finance

On January 5, Securities and Exchange Commission Chairman Christopher Cox announced the appointment of Shelley E. Parratt to serve as Acting Director of the Division Corporation Finance. Ms. Parratt served as Deputy Director of the Division of Corporation Finance since 2003. Ms. Parratt replaces John W. White, who left the SEC to return to private practice.

http://www.sec.gov/news/press/2009/2009-3.htm

Litigation

Non-Parties Enjoined from Filing Bankruptcy Petitions Against Entities in Receivership

The Securities and Exchange Commission brought an action against several individuals and related investment entities (the Wextrust Entities) who allegedly participated in a Ponzi scheme that purportedly defrauded over 1,000 investors of approximately $255 million. Contemporaneous with the filing of the lawsuit, the District Court issued an order (i) appointing a temporary receiver to ascertain the financial condition and manage the assets of the Wextrust Entities, and (ii) enjoining any person or entity from taking action that would interfere with the assets of the Wextrust Entities, including filing any lawsuits, liens, encumbrances or bankruptcy petitions.

Creditors of the Wextrust Entities challenged the enforceability of the order, arguing that the District Court did not have authority to enjoin them, as non-parties, from filing involuntary bankruptcy petitions against the Wextrust Entities.

After noting that there was no Second Circuit authority directly addressing the issue, the District Court found support for its injunction in decisions issued by the Ninth and Sixth Circuits. Drawing from those decisions, the District Court found that its authority to enjoin the non-parties arose from its power over the assets placed in receivership, reasoning that if it could not enjoin them from bringing suit and otherwise contesting receivership assets, the purpose of the receivership would be undermined because the receiver would be unable to control and protect the assets. The District Court further

LITIGATION

For more information, contact:

Alan R. Friedman
212.940.8516
alan.friedman@kattenlaw.com

Brian L. Muldrew
212.940.6581
brian.muldrew@kattenlaw.com

supported its authority to issue the injunction by invoking the rule in the Second Circuit that "once the equity jurisdiction of the district court has been properly invoked by a showing of a securities law violation, the court possesses the necessary power to fashion an appropriate remedy." (*Securities and Exchange Commission v. Byers*, 2008 WL 5236644 (S.D.N.Y.))

Arbitration Award Based on Contract Provision Not Addressed by Parties Upheld

Plaintiff, a vice president of sales and marketing, commenced an arbitration against his employer (i2) alleging that i2 had failed to pay him approximately $2.7 million in sales commissions due under his Account Manager Compensation Plan (the Contract). Following the arbitrator's issuance of an award of $1 million in plaintiff's favor, i2 moved to vacate, or, alternatively, modify the award, arguing that the arbitrator exceed his authority by basing his award on his finding that i2 had breached a section of the Contract that neither party had ever referenced during the arbitration.

The District Court began its analysis by recognizing that judicial review of an arbitration award is "exceedingly deferential" and that, under applicable Fifth Circuit precedent, such an award must be upheld if it "is rationally inferable from the letter or purpose of the underlying agreement." The Court then noted that "no court has yet addressed the question of whether an arbitrator can base his decision in a breach of contract case on a section of the contract that was not specifically referenced in the parties' briefs or during the arbitration."

In upholding the award, the District Court cited a Fifth Circuit case in a related context in which the court ruled that "when considering whether an arbitrator has exceeded his authority in ruling upon a matter not submitted to him, the only question the court is permitted to ask is 'whether the award, however arrived at, is rationally inferable from the contract.'" Applying this standard, the District Court ruled that the arbitrator could have rationally inferred he had the power to base the award on the section of the contract he relied upon. The Court noted that there was no indication that the parties had limited the arbitrator's authority to only those provisions of the Contract that they referenced. Accordingly, the Court upheld the award, finding that (i) the issue presented to the arbitrator was whether i2 had breached the Contract, and (ii) it was reasonable for the arbitrator to infer that he could rest his decision on a different section of the Contract than the one i2 relied upon to support its position. (*VandenAvond v. I2 Technologies, Inc.*, 2008 WL 5336300 (N.D.Tex.))

Broker Dealer

Nasdaq Proposes Limited OATS Exemption for Options Market Makers

Nasdaq submitted a rule proposal to adopt a limited exemption from the Order Audit Trail System (OATS) requirements for bona fide hedging transactions in Nasdaq-listed securities that are part of a Nasdaq member's market making activity in options. The proposed OATS exemption would apply to options market making on any options exchange in any standardized option made available for clearing through the Options Clearing Corporation. According to Nasdaq, because bona fide hedging transactions in equity securities executed by options market makers do not involve customer orders, requiring submission of bona fide hedging transactions in equity securities to OATS does not provide sufficient customer protection or equivalent regulatory benefit to justify the associated expense of reporting. In addition, Nasdaq noted that the relevant information is captured by and available through Nasdaq's electronic delivery system upon request.

http://www.sec.gov/rules/sro/nasdaq/2008/34-59163.pdf

BROKER DEALER

For more information, contact:

Janet M. Angstadt
312.902.5494
janet.angstadt@kattenlaw.com

Gary N. Distell
212.940.6490
gary.distell@kattenlaw.com

Daren R. Domina
212.940.6517
daren.domina@kattenlaw.com

Patricia L. Levy
312.902.5322
patricia.levy@kattenlaw.com

Ross Pazzol
312.902.5554
ross.pazzol@kattenlaw.com

James D. Van De Graaff
312.902.5227
james.vandegraaff@kattenlaw.com

Lance A. Zinman
312.902.5212
lance.zinman@kattenlaw.com

FINRA Proposes Changes to "Manning" Rule

The Financial Industry Regulatory Authority (FINRA) proposed to amend NASD Interpretive Material (IM) 2110-2, commonly referred to as the "Manning" Rule. The proposed amendments would allow member firms to calculate a current inside spread by contacting and obtaining priced quotations from at least two unaffiliated dealers for the purpose of determining the minimum price improvement obligation under "Manning" where there is no published current inside spread. The proposed changes are designed to address an "overly restrictive" result brought about by other recent changes to "Manning" that created tiered standards of price improvement (varying according to the price of a limit order) that are required in order to trade ahead of an unexecuted limit order. For example, under the recent changes, the Rule requires $0.01 price improvement when a member receives a $0.01 limit order if there is no current inside spread, thus effectively prohibiting the member from selling while the customer order is pending. In addition, the filing proposes amendments to allow a member firm to determine the current inside spread by using the best price obtained from at least two unaffiliated dealers on the other side of the quote when there is a one-sided quote.

http://www.sec.gov/rules/sro/finra/2008/34-59138.pdf

CBOE Proposes Rule Change for Trades for Less Than $1

The Chicago Board Option Exchange submitted a proposed rule change amending CBOE's accommodation liquidation procedures to allow transactions to take place at a price that is below $1 per option contract. The proposed rule change temporarily amends the procedures through January 30 to allow transactions to take place in open outcry at a price of at least $0 but less than $1 per option contract. These lower-priced transactions would be traded pursuant to the same procedures applicable to $1 cabinet trades, except that (i) bids and offers for opening transactions would only be permitted to accommodate closing transactions in order to limit use of the procedure to liquidations of existing positions, and (ii) the procedures would also be made available for trading in option classes participating in the Penny Pilot Program. The Securities and Exchange Commission has designated this rule change proposal operative upon filing.

http://sec.gov/rules/sro/cboe/2008/34-59188.pdf

Nasdaq Adopts Policy to Highlight Trade Reports Inconsistent With Prevailing Market

Nasdaq made two companion filings with the Securities and Exchange Commission to adopt a policy of attaching Aberrant Report Indicators to trade reports that Nasdaq determines to be inconsistent with the prevailing market. This policy is substantially similar to the one recently adopted by the New York Stock Exchange (NYSE), as reported in the October 17, 2008, edition of *Corporate and Financial Weekly Digest*. Trades that are marked by the Aberrant Report Indicator are still valid trades, i.e., they were executed and not unwound as in the case of a clearly erroneous trade. Nasdaq's policy, like the NYSE's, includes general numerical guidelines that will be consulted when determining whether trade prices are inconsistent with the prevailing market. The SEC approved Nasdaq's request that the policy become effective immediately. Nasdaq also proposed that the policy be made retroactive to September 1, 2008.

http://www.sec.gov/rules/sro/nasdaq/2008/34-59149.pdf
http://www.sec.gov/rules/sro/nasdaq/2008/34-59151.pdf

Structured Finance and Securitization

Citigroup Announces Support for Mortgage Bankruptcy Reform Act

On January 8, Senator Richard Durbin (D-IL), Senator Christopher Dodd (D-CT), Senator Charles Schumer (D-NY) and Representative John Conyers (D-MI) announced an agreement with Citigroup on legislation that would allow homeowners in bankruptcy to alter the terms of their mortgages. Citigroup has agreed to support the "Helping Families Save Their Homes in Bankruptcy Act," introduced by Senator Durbin on January 6, along with a companion bill that was introduced on the same day in the House of Representatives by Representative Conyers. The original legislation would remove a provision of the bankruptcy law that disallows modifications to mortgage loans on a debtor's principal residence, would extend the time frame debtors are allowed for repayment, and would allow bankruptcy judges to replace escalating variable interest rates with a new interest rate. Citigroup gave its support to the legislation in response to certain changes which have been made, including that only existing mortgages will be eligible, that homeowners will be required to certify that they have attempted to negotiate with their lender regarding loan modifications before filing for bankruptcy, and that only major violations of the Truth in Lending Act will invalidate creditor claims in bankruptcy.

http://durbin.senate.gov/showRelease.cfm?releaseId=306480

CFTC

International Derivatives Clearinghouse Registers as a Derivatives Clearing Organization

On December 22, the Commodity Futures Trading Commission issued an Order granting the application of International Derivatives Clearinghouse, LLC (IDC) for registration as a derivatives clearing organization (DCO) pursuant to Section 5b of the Commodity Exchange Act. As a result of its DCO registration, IDC has authorization to clear interest rates and currency futures contracts, options on futures contracts, commodity options and over-the-counter derivatives. IDC is a subsidiary of International Derivatives Clearing Group, which is 80% owned by NASDAQ OMX Group, Inc.

http://cftc.gov/newsroom/generalpressreleases/2008/pr5591-08.html

CFTC Announces Chicago Mercantile Exchange Certification of Credit Default Swap Clearing

On December 23, the Commodity Futures Trading Commission announced that the Chicago Mercantile Exchange Inc. (CME) has certified plans to clear certain credit default swaps (CDS) through its registered derivatives clearing organization (DCO) clearinghouse. CME has certified that its clearing services will comply with the DCO Core Principles in Section 5b(c)(2) of the Commodity Exchange Act and Part 39 of the CFTC's regulations. The CFTC's decision not to object to CME's certification was also supported by the staff of the Board of Governors of the Federal Reserve System.

http://www.cftc.gov/newsroom/generalpressreleases/2008/pr5592-08.html

CFTC Proposes to Exempt Options and Security Futures on Gold and Silver Products

On November 12, the Commodity Futures Trading Commission proposed to exempt from the Commodity Exchange Act and the regulations thereunder the trading and clearing of certain "options" and "security futures" contracts on iShares COMEX Gold Trust Shares and iShares Silver Trust Shares. The contracts subject

STRUCTURED FINANCE AND SECURITIZATION

For more information, contact:

Eric S. Adams
212.940.6783
eric.adams@kattenlaw.com

Hays Ellisen
212.940.6669
hays.ellisen@kattenlaw.com

Reid A. Mandel
312.902.5246
reid.mandel@kattenlaw.com

CFTC

For more information, contact:

Kenneth Rosenzweig
312.902.5381
kenneth.rosenzweig@kattenlaw.com

Fred M. Santo
212.940.8720
fred.santo@kattenlaw.com

Kevin Foley
312.902.5372
kevin.foley@kattenlaw.com

Lance A. Zinman
312.902.5212
lance.zinman@kattenlaw.com

to the proposed exemption would be traded on national securities exchanges (in the case of options) and on designated contract markets registered as limited purpose national securities associations with the Securities and Exchange Commission (in the case of security futures), and would be cleared through the Options Clearing Corporation, which is registered with the CFTC as a derivatives clearing organization, in its capacity as a registered securities clearing agency.

http://www.cftc.gov/stellent/groups/public/@lrfederalregister/documents/file/e8-26815a.pdf

CFTC Seeks Comments on Contract Market and Derivatives Clearing Organization Application

The Commodity Futures Trading Commission is seeking public comment on an application by Cantor Fitzgerald, L.P. for the designation of Cantor Futures Exchange, L.P. as a contract market and the registration of Cantor Clearinghouse, L.P. as a derivatives clearing organization. The deadline for comments is January 28.

http://www.cftc.gov/newsroom/generalpressreleases/2009/pr5595-09.html

Banking

Banking Agencies Issue Interagency Questions and Answers on Community Reinvestment

On January 6, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency and the Office of Thrift Supervision (collectively, the Banking Agencies) issued new and revised Interagency Questions and Answers Regarding Community Reinvestment (the Community Reinvestment Guidance) intended to supplement existing guidance on the same topic. The Banking Agencies had released proposed supplemental questions and answers in 2007.

According to the accompanying press release, the Banking Agencies' intent is for the Community Reinvestment Guidance to encourage financial institutions to participate in foreclosure prevention programs that have the objective of providing affordable, sustainable, long-term loan restructurings or modifications for homeowners who are facing foreclosure on their primary residences.

With adoption of the Community Reinvestment Guidance, the Banking Agencies adopted nine new questions and answers that were originally proposed in 2007 and also adopted substantive changes to 14 existing questions and answers that had appeared in prior guidance on the topic. The Community Reinvestment Guidance also proposed one new and two revised questions and answers. The proposed revisions to the two existing questions and answers would allow pro rata consideration in certain circumstances for an activity that provides affordable housing targeted to low- or moderate-income individuals. The newly proposed question and answer provides examples of how an institution can determine that community services it provides are targeted to low- and moderate-income individuals. Comments with respect to such proposals are due on March 9.

http://www.ots.treas.gov/?p=PressReleases&ContentRecord_id=ac680dd5-1e0b-8562-eba9-273c723e74bd&ContentType_id=4c12f337-b5b6-4c87-b45c-838958422bf3

BANKING

For more information, contact:

Jeff Werthan
202.625.3569
jeff.werthan@kattenlaw.com

Terra K. Atkinson
704.344.3194
terra.atkinson@kattenlaw.com

Christina J. Grigorian
202.625.3541
christina.grigorian@kattenlaw.com

Adam Bolter
202.625.3665
adam.bolter@kattenlaw.com

UK Developments

UK Treasury Considers Modernization of Insolvency Protections for Financial Markets

On December 29, the UK Treasury published a summary of responses to its consultation on its proposals to reform Part 7 of the UK Companies Act 1989 and related legislation. Part 7 of the Companies Act 1989 modifies the UK's general insolvency law to provide systemic protection for recognized investment exchanges and recognized clearinghouses in the event of a default by one of their members

Respondents generally supported the proposals which relate to: (i) provision for the operation of default funds and cross-margining arrangements; (ii) permitting the use of a defaulting member's house account surpluses to meet any client account deficits; (iii) an expansion of the definition of a "market contract"; (iv) provisions designed to ensure that client money provisions of other jurisdictions are honored; and (v) the need to reflect certain amendments to UK insolvency law relating to administration.

The summary includes a technical explanation of the amendments made to the draft regulations as a result of responses to the consultation, and Annex B contains the amended draft Financial Markets and Insolvency Regulations 2009.

The Treasury intends to lay the regulations before the UK Parliament as soon as possible after the end of January.

www.hm-treasury.gov.uk/consult_companiesact1989.htm

FSA Proposes to Lift Ban on Short Selling

On January 5, the UK Financial Services Authority (FSA) announced a consultation on a proposal to allow its ban on short sales of UK financial sector stocks to expire on January 16. The FSA also proposed to extend its temporary disclosure regime for significant net short positions in UK financial sector company stocks to June 30. The short position disclosure obligations will continue to apply only to UK financial sector companies.

The temporary ban on short selling of financial sector stocks was introduced in September 2008. The FSA has now stated that it considers that the risk posed by short selling in terms of potential market abuse and creating disorderly markets has declined such that it is not appropriate to renew the ban. However, the FSA emphasized that it will monitor the position closely and will reintroduce the short sales ban if it is warranted. If necessary, this will be done without further consultation.

Under the proposals, the FSA will continue the disclosure regime applicable to short sales of UK financial sector stocks until June 30. The threshold for disclosure would remain unchanged at 0.25%. The thresholds for additional disclosures would change from the current position, under which disclosure of all changes to any net short position must be disclosed. Under the FSA's proposals, further disclosures will be required only as increments of 10 basis points are crossed (in other words as a net short position reaches 0.35%, 0.45%, etc).

The consultation will close on January 9 to enable the new measures to be in place on January 16.

The FSA has also announced that it will publish a separate consultation paper no later than February 5 setting out its proposals for a longer-term short-selling regime.

www.fsa.gov.uk/pubs/cp/cp09_01.pdf

UK DEVELOPMENTS

For more information, contact:

Martin Cornish
44.20.7776.7622
martin.cornish@kattenlaw.co.uk

Sam Tyfield
44.20.7776.7640
sam.tyfield@kattenlaw.co.uk

Edward Black
44.20.7776.7624
edward.black@kattenlaw.co.uk

Sean Donovan-Smith
44.20.7776.7625
sean.donovan-smith@kattenlaw.co.uk

FSA Propose to Amend Integrated Regulatory Reporting Regime

On January 6, the UK Financial Services Authority (FSA) published *Quarterly Consultation No 19* (CP09/2), which proposes amendments to Chapter 16 of the FSA's Supervision manual (SUP) relating to Integrated Regulatory Reporting requirements.

The proposed amendments follow enquiries and requests for clarification made to the FSA on its new reporting system known as "GABRIEL". The enquiries and requests identified some inconsistencies and duplications which the FSA now wishes to resolve. The proposed amendments affect the following provisions: (i) various rules and guidance set out at SUP 16.12.1R to SUP 16.12.33R; and (ii) SUP 16 Annex 24R (reporting forms) and SUP 16 Annex 25G (guidance on completing the forms).

The deadline for comments is March 6.

www.fsa.gov.uk/pages/Library/Policy/CP/2009/09_02.shtml

FSA Launches Further Insider Dealing Prosecution

On January 7, the UK Financial Services Authority (FSA) charged Neil Rollins at the City of Westminster Magistrates' Court with insider dealing and money laundering offenses.

The FSA alleges that Mr. Rollins disposed of approximately 74,000 shares of PM Group plc between August and September 2006 while in possession of inside information and that he encouraged Louisa Rollins to deal in shares in the Group. The money laundering charges relate to the transfer of criminal property on various dates in November 2006 to an account in the name of David Rollins while knowing or suspecting that it represented the proceeds of insider trading.

The Magistrates Court held that the case was suitable for trial before the Crown Court, and proceedings were adjourned until February 18.

www.fsa.gov.uk/pages/Library/Communication/PR/2009/002.shtml

* Click here to access the *Corporate and Financial Weekly Digest* archive.

Katten

Katten Muchin Rosenman LLP

www.kattenlaw.com

Charlotte
401 S. Tryon Street
Suite 2600
Charlotte, NC 28202-1935
704.444.2000 tel
704.444.2050 fax

Chicago
525 W. Monroe Street
Chicago, IL 60661-3693
312.902.5200 tel
312.902.1061 fax

Irving
5215 N. O'Connor Boulevard
Suite 200
Irving, TX 75039-3732
972.868.9058 tel
972.868.9068 fax

London
1-3 Frederick's Place
Old Jewry
London EC2R 8AE
+44.20.7776.7620 tel
+44.20.7776.7621 fax

Los Angeles
2029 Century Park East
Suite 2600
Los Angeles, CA 90067-3012
310.788.4400 tel
310.788.4471 fax

New York
575 Madison Avenue
New York, NY 10022-2585
212.940.8800 tel
212.940.8776 fax

Palo Alto
260 Sheridan Avenue
Suite 450
Palo Alto, CA 94306-2047
650.330.3652 tel
650.321.4746 fax

Washington, DC
2900 K Street, NW
Suite 200
Washington, District of Columbia 20007-5118
202.625.3500 tel
202.298.7570 fax