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SEC/CORPORATE

SEC Issues New Interpretations Related to Executive Compensation and Say-on-Pay Reporting

On July 8, the Securities and Exchange Commission's Division of Corporation Finance issued new Compliance and Disclosure Interpretations (C&DIs) on executive compensation disclosure and reporting with respect to the frequency of shareholder advisory votes on executive compensation (i.e., "say on pay").

The SEC's new guidance included the following:

- C&DI 121A.04 states that with respect to a company's decision as to how frequently it will include say-on-pay advisory votes in its proxy materials, an issuer may report its decision in a periodic report (i.e., Form 10-Q or Form 10-K) filed on or before the date that the Item 5.07 Form 8-K is due. If the issuer reports the voting results of an annual meeting in a Form 10-Q or Form 10-K, the issuer may file a new Item 5.07 Form 8-K, rather than an amended Form 10-Q or Form 10-K, to report its decision as to how frequently it will include say-on-pay votes in its proxy materials. However, if an issuer reports its annual meeting voting results in a Form 8-K and also intends to report its decision as to the frequency of say-on-pay votes in a Form 8-K, such decision must be reported as an amendment to the original Form 8-K, rather than as a new Form 8-K.

- C&DI 121A.03 states that under Item 5.07(b) of Form 8-K, it is not necessary to disclose the number of broker non-votes with respect to advisory votes on the frequency of say-on-pay advisory votes (although an issuer may disclose such information if the issuer believes such information would be useful to investors).

- C&DI 117.07 clarifies that under Item 402 of Regulation S-K, companies may omit disclosure of disability plans to the extent the disability plans do not discriminate in scope, terms or operation in favor of executive officers or directors and are available generally to all salaried employees.

- C&DI 118.08 clarifies that where non-generally accepted accounting principles (GAAP) financial measures are presented in Compensation Discussion & Analysis or other proxy statement disclosure for any purpose other than to disclose performance target levels, relief from the requirements of Regulation G and Item 10(e) (including the requirement that such non-GAAP measures be reconciled to comparable GAAP measures) under Instruction 5 to Item 402(b) of Regulation S-K is not available. However, in these circumstances, the SEC will not object if a registrant includes the GAAP reconciliation and other required information in an annex to the proxy statement, provided the registrant also includes a prominent cross-reference to such annex (or, if applicable, a cross-reference to the pages of the company's Form 10-K containing the GAAP reconciliation and other required information).

- C&DI 119.28 clarifies that where target levels for performance-based equity compensation are set at the beginning of Year 1, but awards are not granted until performance results for Year 1 are determined in Year 2, the grant date fair value for equity awards must be reported based on the *probable* outcome of the

performance condition as of the grant date, even if the *actual* outcome is known by the time the proxy statement is filed, in accordance with Instruction 3 to Item 402(c)(2)(v) and (vi) of Regulation S-K.

Click here to view C&DI 121A.03.
Click here to view C&DI 121A.04.
Click here to view C&DI 117.07.
Click here to view C&DI 118.08.
Click here to view C&DI 119.28.

BROKER DEALER

SEC Announces Adoption of Interim Final Temporary Rule for Broker-Dealers Engaging in a Retail Forex Business

On July 13, the Securities and Exchange Commission adopted interim final temporary Rule 15b12-1T to allow a registered broker-dealer to engage in a retail forex business until July 16, 2012, provided that the broker-dealer complies with the Securities Exchange Act of 1934, the rules and regulations thereunder, and the rules of the self-regulatory organization(s) of which the broker-dealer is a member, insofar as they are applicable to retail forex transactions.

Under the Dodd-Frank Wall Street Reform and Consumer Protection Act, certain forex transactions with persons who are not "eligible contract participants" (commonly referred to as "retail forex transactions") with a registered broker or dealer will be prohibited as of July 16, 2011, in the absence of the SEC adopting this interim Rule 15b12-1T to allow such transactions. According to the SEC, Rule 15b12-1T is intended to preserve the existing regulatory structure for broker-dealers while providing the SEC with an opportunity to receive comments and evaluate whether to prescribe additional rules and to further consider investor protection concerns as they affect the regulatory treatment of retail forex transactions by broker-dealers. Comments are due to the SEC 60 days after publication in the *Federal Register*.

Click here to read Securities and Exchange Commission Release No. 34-64874.

CBOE Announces Registration Extension for New WebCRD Categories

On July 8, the Chicago Board Options Exchange (CBOE) announced a new registration deadline of September 19 for individuals seeking to register for new WebCRD categories. Effective June 20, three new registration categories, including (1) Proprietary Trader – PT, (2) Proprietary Trader Compliance Officer – CT, and (3) Proprietary Trader Principal – TP, became available to CBOE and CBOE Stock Exchange Trading Permit Holders on WebCRD. All of the new registration categories are subject to certain qualification and examination requirements. The original deadline for completion of such qualification and examination requirements was August 12.

Click here to read Regulatory Circular RG11-088.
Click here to read a summary of the new WebCRD categories as reported in the July 8 edition of *Corporate and Financial Weekly Digest*.

PRIVATE INVESTMENT FUNDS

SEC Raises "Qualified Client" Thresholds

On July 12, the Securities and Exchange Commission issued an order raising the thresholds for determining who is a "qualified client" for purposes of Rule 205-3 under the Investment Advisers Act of 1940. Rule 205-3 exempts an investment adviser from the prohibition against charging a client performance fees in certain circumstances, including when the client is a qualified client. Under the order, a qualified client is one who: (1) has at least $1 million under the management of the adviser immediately after entering into the advisory contract, or (2) the adviser reasonably believes has a net worth of more than $2 million at the time the contract is entered into. These thresholds were raised from $750,000 and $1,500,000, respectively, to adjust for inflation, as required by the Dodd-Frank Wall Street Reform and Consumer Protection Act. The SEC's order becomes effective on September 19.

In its initial proposal to increase the qualified client thresholds, the SEC also proposed, among other things, to: (1) exclude the value of a person's primary residence from the test of whether a person has sufficient net worth to be considered a qualified client, and (2) add certain transition provisions to the rule to allow an investment adviser and its clients to maintain existing performance fee arrangements that were permissible when the advisory contract was entered into, even if performance fees would not be permissible under the contract if it were entered into at a later date. The SEC has not yet addressed these additional proposals.

Click here to read the SEC's order.
Click here to read the SEC's proposed amendments to Rule 205-3.

GAO Reports on the Feasibility of SRO for Private Fund Advisers

On July 11, the U.S. Government Accountability Office (GAO) released a report on the feasibility of forming a self-regulatory organization (SRO) to provide primary oversight of private fund advisers. The report was part of a mandate by the Dodd-Frank Wall Street Reform and Consumer Protection Act to address the potential gap in the regulation of private fund advisers. In preparing the report, GAO reviewed federal securities laws, the recently completed Securities and Exchange Commission study on the investment adviser examination program, past regulatory and legislative proposals to create an SRO for investment advisers, and associated comment letters. GAO believes that the formation of a private fund adviser SRO is feasible but includes challenges such as the passage of new legislation, raising sufficient start-up capital and reaching agreements on fee and governance structures. The report also notes that while a private fund adviser SRO could supplement and help the SEC's oversight of investment advisers, the fragmentation between regulation of private fund advisers and non-private fund advisers could lead to regulatory gaps, duplication and inconsistencies.

Click here to read the GAO report.
Click here to read a summary of the SEC's study on the investment adviser examination program in the January 21 edition of *Corporate and Financial Weekly Digest*.
Click here to read a summary of industry comments on the desirability of a private fund adviser SRO in the November 12, 2010, edition of *Corporate and Financial Weekly Digest*.

DERIVATIVES

ISDA Publishes Long-Awaited Equity Derivatives Definitions

On July 8, the International Swaps and Derivatives Association (ISDA) published its 2011 Equity Derivatives Definitions. The 2011 Definitions were developed with significant non-dealer participation, and they allow for a great deal of flexibility in the way parties allocate risks and burdens in their over-the-counter equity derivative transactions. The 2011 Definitions consist of a main book of definitions that revises and expands the 2002 Equity Derivatives Definitions and an appendix that contains tables setting out possible elections, consequences and fallbacks for different types of trades. Although parties are now free to incorporate the 2011 Definitions into their trades, it is expected that the 2011 Definitions will be introduced incrementally via the adoption by ISDA of standard matrices of terms from the definitions for different types of transactions; the ISDA working group is expected to introduce by August 31 transaction matrices for U.S. and EU Index Variance Swaps. The publication of the 2011 Definitions will not, without further action by the parties, affect existing confirmations and other documents that incorporate either the 1996 or the 2002 versions of the ISDA Equity Derivatives Definitions.

Further information, and copies of the 2011 Definitions, are available on the ISDA website here.

CFTC

CME, CBOT and NYMEX Revise Customer Confirmation Rule

The CME Group has announced amendments to CME, CBOT and NYMEX Rule 957, which specifies the information that must be included in a clearing member's confirmations to its customers, to require that confirmation statements "show facts relevant to the economic terms of the transaction." The changes to Rule 957 are effective immediately, and are intended to broaden the scope of the rule to include types of information that may be necessary to confirm over-the-counter swaps transactions.

The CME Group advisory notice announcing the rule change may be found here.

CFTC Proposes Order Providing Exemptive Relief from Certain Dodd-Frank Provisions

The Commodity Futures Trading Commission has issued an Order, essentially in the form proposed, providing temporary relief from certain swap-related provisions of Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act that would otherwise take effect on July 16. The *Federal Register* release accompanying the Order groups the provisions of Title VII as to which the CFTC has regulatory responsibility into four broad categories:

1) provisions that, by their terms, do not take effect without the adoption of implementing rules;
2) self-effectuating provisions that include references to terms that require further definition;
3) self-effectuating provisions that do not reference terms requiring further definition and that repeal current provisions of the Commodity Exchange Act (CEA); and
4) other self-effectuating provisions.

The Order provides relief for categories 2 and 3 above. The remaining provisions will take effect either on (1) July 16 (in the case of category 4 above), or (2) upon the effective date of the applicable final implementing rules, which can be no earlier than 60 days following their adoption (in the case of category 1 above).

With respect to category 2 provisions, the Order temporarily exempts persons from complying with many provisions of the CEA that reference the terms "swap," "swap dealer," "major swap participant" or "eligible contract participant," each of which is subject to further rulemaking by the CFTC.

With respect to category 3 provisions, the Order temporarily exempts specified over-the-counter transactions in exempt and excluded commodities, effectively preserving the current regulatory safe harbors applicable to such transactions.

The Order includes a "sunset" provision, which provides that the exemptive relief will expire upon the earlier of either (1) December 31, or (2) the effective date of the applicable final rules. If necessary, the CFTC may extend the period beyond December 31.

Concurrently, the CFTC staff has adopted a no-action position with respect to three provisions of the CEA that take effect on July 16 and for which exemptive relief is not available: (1) Section 4s(l), which requires swap dealers and major swap participants to segregate collateral with respect to certain uncleared swaps; (2) Section 4s(k), which specifies the duties of a chief compliance officer for swap dealers and major swap participants; and (3) Section 5b(a), which prohibits any clearing organization from clearing swaps unless it is registered with the CFTC.

A copy of the Order, which includes charts identifying the provisions of the Dodd-Frank Act that fall within each category above, and the no-action position may be found here.

INVESTMENT COMPANIES AND INVESTMENT ADVISERS

Please see "SEC Raises 'Qualified Client' Thresholds" and "GAO Reports on the Feasibility of SRO for Private Fund Advisers" in **Private Investment Funds** above.

LITIGATION

Rule 10b-5 Applies to Transfers of Foreign Securities That Close in the U.S.

The U.S. Court of Appeals for the Eleventh Circuit recently vacated a district court's dismissal of a complaint for lack of subject matter jurisdiction, finding that the district court erred in holding that Section 10(b) and Rule 10b-5 did not apply to a sale of shares in a foreign corporation that closed in the United States.

Plaintiff Quail Cruises Ship Management Ltd. brought a claim for securities fraud against Agencia de Viagens CVC Tur Limitada (CVC), alleging that CVC orchestrated a series of misrepresentations in order to induce Quail to purchase the *M/V Pacific*, a boat once featured in *The Love Boat* television series. The acquisition was effected through the transfer of shares of Templeton International Inc., whose principal asset was the *M/V Pacific*. Because

the Templeton stock was not listed on a United States exchange, pursuant to the Supreme Court's decision in *Morrison v. Nat'l Australia Bank Ltd.*, Section 10(b) would only reach the transaction if the sale occurred here.

Applying *Morrison*, the Eleventh Circuit held that the sale occurred in the United States because the complaint alleged that the transaction closed here. In particular, the complaint alleged that "the acquisition of the Templeton stock closed in Miami, Florida, on June 10, 2008, by means of the parties submitting the stock transfer documents by express courier into this District." In so holding, the court noted that the purchase and sale agreements specifically contemplated that the transfer of shares would not be complete until this closing occurred. (Quail *Cruises Ship Management Ltd. V. Agencia de Viagens CVC Tur Limitada,* Nos. 10-14129, 10-14253, 2011 WL 2654004 (11th Cir. July 8, 2011))

Alleged Financial Distress Insufficient to Support Grant of Preliminary Injunction

The Delaware Court of Chancery denied a request for a preliminary injunction, finding that allegations of "financial distress" failed to demonstrate the imminent, irreparable harm required to obtain immediate injunctive relief.

Defendant Cementos Portland Valderrivas held a majority stake in both Uniland S.A. and Giant Cement Holding, Inc. In December 2010, Cementos sold Giant to Uniland. Plaintiff Sagarra Inversiones, S.L., a minority shareholder of Uniland, alleged that the acquisition price was improperly inflated as a result of Cementos's self-dealing and position on both sides of the transaction. Under the stock purchase agreement governing the acquisition, the merger consideration was to be paid in installments. Sagarra moved for interim injunctive relief to prevent the payment of any additional funds under the agreement.

In an attempt to demonstrate that it would be irreparably harmed if the injunction was not granted, Sagarra alleged that Cementos was in financial distress and having difficulty in satisfying its financial covenants and, as a result, would be unable to satisfy a money judgment if Sagarra were to prevail on its claims. The Court of Chancery denied the request for a preliminary injunction. The court ruled that even if the threat of defendant's insolvency could satisfy the irreparable harm standard, Sagarra's failure to demonstrate "any specific or imminent threat that Cementos will be rendered insolvent" was fatal to its application for injunctive relief. (*Sagarra Inversiones, S.L. v. Cementos Portland Valderrivas S.A.,* No. 6179-VCN (Del. Ch. July 7, 2011))

BANKING

Federal Reserve Publishes Interchange Small-Bank Exemption Lists

The Federal Reserve on July 12 published lists of banks that it believes are subject to—and are not subject to—the debit card interchange rule's small bank exemption for issuers with under $10 billion in assets. The lists, which are intended to help payment card networks determine which issuers must adhere to the rule's price caps, are part of the Federal Reserve's attempt "to reinforce the exemption and monitor its effectiveness." The statute exempts any debit card issuer that, together with its affiliates, has assets of less than $10 billion. The Federal Reserve plans to update the lists annually. The interchange rule becomes effective October 1.

Read more.

Consumer Financial Protection Bureau Outlines Bank Supervision Approach

The Consumer Financial Protection Bureau (CFPB) on July 12 outlined its approach to supervising the 111 large banks with more than $10 billion in assets that it will oversee beginning July 21. "Starting on July 21, we will be a cop on the beat—examining banks and protecting consumers," said Treasury Department special adviser Elizabeth Warren, who is overseeing the establishment of the CFPB.

Examiners will be managed out of satellite offices in Chicago, New York, San Francisco, and Washington, D.C. According to the release, "Each of these satellite offices will be the nexus for CFPB supervision in their respective areas of the country. Having examiners and field managers focused on these regions will help ensure that the CFPB understands the business practices and dynamics in different markets throughout the country." The Bureau said it will conduct periodic examinations for most of the banks it supervises. But for the largest and most complex

banks, the CFPB will implement a year-round supervision program that will be customized to reflect the consumer protection and fair-lending risk profile of the organization.

In the weeks following July 21, CFPB examiners and managers will become familiar with the structures, business strategies, operations and risks of the banks they will supervise; coordinate the bureau's efforts with federal and state regulatory agencies; finalize plans to supervise and examine institutions under its jurisdiction; and begin conducting the agency's first round of on-site examinations.

"This process will begin remotely in most instances, and CFPB examiners will then begin on-site reviews at the supervised institutions to continue their work," the Bureau said. "Over the next several weeks, the CFPB will conduct further outreach to banks that fall under its jurisdiction. The CFPB will provide additional information via letter to the 111 institutions, and will conduct informational roundtables starting in early August." The CFPB stated it will post on its website the initial phase of its Examination Manual, which is the field guide for examiners supervising both banks and other consumer financial services companies. The publication of the manual will be accompanied by a general invitation for feedback and suggestions for improvements from the banking industry, nonbank financial services companies, federal and state agencies, consumer and community groups, and the general public.

Sounding a word of warning, the Bureau indicated that "[i]f a company is not fully compliant, the CFPB will seek corrective actions, including strengthening the company's programs and processes to ensure that such violations do not recur and, where appropriate, that remedies are instituted. When necessary examiners will coordinate and work closely with CFPB's enforcement staff to implement appropriate enforcement actions to address harm to consumers."

Read more.

EU DEVELOPMENTS

ESMA Publishes Consultation Paper on AIFMD

On July 13, the European Securities and Markets Authority (ESMA) published a consultation paper on possible Level 2 implementing measures for the Alternative Investment Fund Managers Directive (AIFMD). The paper is entitled *ESMA's draft technical advice to the European Commission on possible implementing measures of the Alternative Investment Fund Managers Directive.*

The ESMA consultation sets out ESMA's proposals for advice to the European Commission for Level 2 regulations under AIFMD and also contains its commentary on the proposals as well as an Annex 1 which lists 72 questions posed by ESMA to market participants and other "external stakeholders." It follows on from the Discussion Paper that ESMA issued on April 15.

ESMA's general approach has been (as far as possible) to align AIFMD operational requirements with existing provisions in the EU Undertakings for Collective Investment in Transferable Securities Directive (2009/65/EC) (UCITS IV) and the Markets in Financial Instruments Directive (2004/39/EC) (MiFID).

Key issues addressed under the consultation include: general provisions, authorization and operating conditions, initial capital and own funds, general principles and organizational requirements, conflicts of interest, risk management, liquidity management, valuation, delegation of AIFM functions, depositaries, transparency requirements, leverage, annual reporting, disclosure to investors and supervision.

The response deadline is September 13, and in the light of feedback received, ESMA will finalize its proposals with a view to submitting its advice to the European Commission by November 16.

Read more.

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