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Corporate and Financial Weekly Digest

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SEC/CORPORATE

Treasury Department Proposes New "Say-on-Pay" Legislation

On July 16, the U.S. Treasury Department delivered draft "say-on-pay" legislation to Congress that would require that all publicly traded companies allow shareholders a non-binding vote on executive compensation as disclosed in the company's proxy statement for annual meetings held after December 15.

As proposed, the disclosures subject to a shareholders' vote would include tabular data summarizing salary, bonuses, stock and option awards and total compensation for the issuer's senior executive officers and narrative summaries of golden parachute and pension compensation, and of the board of directors' compensation decisions. Additionally, the proposed legislation would require, in connection with a merger or acquisition of an issuer, a separate stockholder vote on golden parachutes provided to executives in connection with such merger or acquisition. Issuers would be required to include and clearly disclose in their soliciting materials the exact amounts senior executive officers would receive if the merger or acquisition is completed.

The Treasury noted that similar regulations have been adopted in the United Kingdom and that several public companies in the United States have voluntarily submitted to "say-on-pay." The Treasury believes that increased dialogue between shareholders and issuers has led directly to the modification of compensation practices.

Read more.

Treasury Department Proposes New Compensation Committee Standards

On July 16, the U.S. Treasury Department delivered draft legislation to Congress that would create stringent requirements for the compensation committees of issuers that are listed on national securities exchanges. As proposed, the legislation would require that each director serving on a compensation committee not be an affiliate of the issuer or accept any consulting or advisory fee of any kind from the issuer, similar to the Sarbanes-Oxley Act requirements imposed on audit committee members. Compensation committees would also be granted the authority and funding to retain and oversee independent compensation consultants and legal advisors. The legislation would require such outside compensation consultants or legal advisors to meet independence standards promulgated by the Securities and Exchange Commission. Finally, issuers would be required to disclose in their proxy and soliciting materials whether their compensation committees have retained independent compensation consultants and, if not, the reason for failing to do so.

Read more.

LITIGATION

Shareholders Did Not Breach Fiduciary Duties Owed to Fellow Shareholders

Defendants and plaintiffs owned interests in Twin City Minerals (Twin City), a company whose only asset was a 50% ownership in Superior Minerals (Superior). Pursuant to a stock purchase agreement, defendants acquired plaintiffs' interest in Twin City. Shortly thereafter, defendants purchased the remaining 50% interest in Superior from Aggregate Industries (Aggregate).

Plaintiffs sued, alleging, among other things, that defendants breached their fiduciary duties by not disclosing to plaintiffs information material to the sale of their interest in Twin City prior to entering into the stock purchase agreement. The court (applying Minnesota law) ruled that shareholders of closely held corporations, such as Twin City, owe fiduciary duties to each other, including a duty to disclose material information. However, following a non-jury trial, the court rejected plaintiffs' contention that defendants had breached their fiduciary duty to plaintiffs.

Plaintiffs claimed that defendants violated their fiduciary duty by failing to make multiple disclosures of material information. For example, plaintiffs claimed that defendants failed to disclose that Aggregate had decided not to provide further financial support to Superior, which would adversely impact Superior's ability to complete a necessary debt refinancing. The court found that defendants were under no duty to disclose such information because defendants legitimately did not believe Aggregate's statements. Similarly, the court held that defendants did not breach their fiduciary duties by failing to disclose that Aggregate had inquired, just weeks before execution of the stock purchase agreement, whether defendants were interested in buying Aggregate's stake in Superior. After considering both the "magnitude" of the potential buyout and its "probability," the court ruled that because the probability "of the buyout was remote and speculative at the time of execution of the stock purchase agreement," the inquiry was not a material fact that required disclosure. As a final example, the court also rejected the plaintiffs' contention that defendants' failure to disclose that alternative financing not requiring any guarantees was available violated their fiduciary duty. Although such financing was obtained weeks after execution of the stock purchase agreement, the court found that no evidence had been produced at trial establishing that such financing was available prior to execution of the stock purchase agreement. (*Dunning v. Bush*, 2009 WL 1964994 (S.D. Iowa July 8, 2009))

Court Grants SEC's Motion for Permanent Injunction

Defendant, the president and CEO of a publicly traded wireless company, maintained an undisclosed ownership interest in an offshore company. Over a three-year period, the defendant directed the wireless company to transfer a total of $348,000 to his offshore corporation on 29 separate occasions without disclosing these transfers on the wireless company's Form 10-KSB annual reports. After defendant pled guilty to securities fraud and tax evasion charges in a related criminal proceeding, the Securities and Exchange Commission sought a permanent injunction against defendant from committing future violations of the Securities Exchange Act.

The court granted the permanent injunction, ruling that the SEC had met its burden of showing that there was a reasonable likelihood of future violations if the injunction was not entered. In making this determination, the court considered the following factors: the degree of scienter involved, the isolated or recurrent nature of the infraction, the defendant's recognition of the wrongful nature of his conduct, the likelihood that future violations might occur, and the sincerity of the defendant's assurances against future violations.

The court determined that each factor favored the injunction. First, the court found that a high degree of scienter was present, because the defendant admitted he knowingly and willfully committed securities fraud in his criminal case plea agreement. Second, the court found that the recurrent nature of the infraction factor weighed in favor of granting an injunction. Although the defendant admitted to committing only one securities law violation, the 29 illegal wire transfers demonstrated a continuous pattern of deceit. Third, because the defendant was a corporate officer who had a duty to make truthful, accurate reports, the court found that his claims that his actions were committed in ignorance of his obligations rang hollow. Accordingly, the court ruled that both the recognition of the wrongful nature of defendant's conduct and the sincerity of his assurances against future violations factors weighed in favor of the injunction. Finally, the court found that the likelihood of future violations factor weighed slightly in favor of the injunction because the defendant, who stated that he would not seek a position with reporting and accounting responsibilities, never stated that he would be unwilling to accept such a position. (*SEC v. Hilsenrath*, 2009 WL 1855283 (N.D. Cal. June 29, 2009))

BROKER DEALER

CBOE Proposes to Amend Rule 8.7 (Obligations of Market-Makers)

The Chicago Board Options Exchange, Inc. (CBOE) is proposing to amend Rule 8.7, Obligations of Market-Makers, to: (i) eliminate the provision providing for bids (offers) to be no more than $1 lower (higher) than the last preceding transaction plus or minus the aggregate change in the last sale price of the underlying, and (ii) modify the provision pertaining to trades that are more than $0.25 below parity.

Rule 8.7 currently provides, in part, that Market-Makers are expected ordinarily, except in unusual market conditions, not to bid more than $1 lower or offer more than $1 higher than the last preceding transaction price for the particular option contract plus or minus the aggregate change in the last sale price of the underlying security since the time of the last preceding transaction for the particular option contract (the "one point" rule). In addition, Market-Makers are expected ordinarily, except in usual market conditions, to refrain from purchasing a call option or a put option at a price more than $0.25 below parity. In the case of calls, parity is measured by the bid in the underlying security, and in the case of puts, parity is measured by the offer in the underlying security (the "parity" rule).

First, the CBOE is proposing to eliminate the one point rule because, as the CBOE points out, various market changes have rendered the rule obsolete and unnecessary. Second, at this time the CBOE is proposing to retain the parity rule as a guideline but to modify it to provide that an amount larger than $0.25 may be appropriate when considering the particular market conditions (not just unusual market conditions as the rule currently states). The rule is also being revised to provide that the $0.25 guideline may be increased, or the parity rule waived, by the CBOE on a series-by-series basis. The CBOE believes that revising the $0.25 parity rule in this manner modernizes the guideline to reflect market changes (including those discussed above) and will provide more flexibility to take into consideration the particular trading in a security, including but not limited to the underlying market price, market conditions, and applicable minimum bid/ask width requirements for a given options series.

Read more.

NYSE's Proposal to Decommission the DPTR Reporting Requirement

The New York Stock Exchange LLC (NYSE) proposes to implement the previously approved decommissioning of the requirement that member organizations report program trading activity via the Daily Program Trading Report (DPTR). Because certain entities previously used DPTR data, the NYSE delayed implementing the decommissioning of the DPTR requirement to provide adequate time to coordinate with such entities. The proposed rule change would require member organizations to file the DPTR with respect to the last trade on July 10, and therefore the last required date to submit the DPTR was July 14.

In lieu of DPTR, the NYSE will utilize existing account type indicator data—which captures program trade information for those orders that are submitted to and executed on the NYSE—to report to the Securities and Exchange Commission on a weekly basis the program trading statistics for portions of program trades executed on the NYSE. Accordingly, beginning on July 23, the NYSE will provide the SEC with its weekly statistics on program trading based on account type indicator data rather than DPTR data. Similarly, at the same time, the weekly statistics regarding program trades that the NYSE provides to media outlets will also be derived from account type indicator data rather than the DPTR.

Read more.

FINRA Proposes New Outside Business Activities Rule

The Financial Industry Regulatory Authority is proposing to adopt a new FINRA Rule 3270 regarding outside business activities. The proposed rule is similar to existing NASD Rule 3030 but includes minor changes. The FINRA filing also deletes existing NYSE Rule 346 and its interpretations. The proposed FINRA rule would expand the obligations imposed under NASD Rule 3030, which requires prompt written notice to a member firm before engaging in an outside business activity, to require that registered representatives provide prior written notice to their member firms. Proposed Rule 3270 retains the exemptions in NASD Rule 3030 for "passive investments" and activities subject to the requirements of NASD Rule 3040.

Read more.

PRIVATE INVESTMENT FUNDS

Please see "Administration Bill Would Require Managers of Hedge and Other Private Funds to Register as Investment Advisors" in **Investment Companies and Investment Advisors** below.

OTC DERIVATIVES

ISDA Opens Small Bang Protocol for Adherence

The International Swaps and Derivatives Association (ISDA) has published a protocol (Small Bang Protocol) which will permit adhering parties to incorporate a new Restructuring Supplement to the 2003 ISDA Credit Derivatives Definitions into existing and new credit default swap (CDS) contracts. In general, the Supplement permits CDS transactions that include restructuring as a credit event to be settled through the auction process that has been hardwired into most CDS transactions.

This is a positive development for firms that trade CDS on European names for two reasons. First, the bankruptcy laws in Europe vary significantly from country to country, and most of these laws do not permit companies to restructure their debt obligations in the context of a bankruptcy (i.e., it is necessary to include restructuring as a credit event under CDS transactions because the bankruptcy credit event does not necessarily encompass the restructuring of debt obligations). In addition, the Basel II capital adequacy rules provide banks with additional capital relief if their CDS transactions include restructuring as a credit event.

Under the Small Bang Protocol, an ISDA Determinations Committee will determine whether there has been a restructuring credit event. If this determination is in the affirmative, CDS contracts may be grouped into as many as nine possible buckets depending on maturity. The Determinations Committee will decide which bonds or loans will be deliverable into which maturity buckets. This process is expected to take about two weeks. ISDA will publish the lists of maturity buckets and their deliverables, and buyers of protection or sellers of protection will then have five business days to decide whether to trigger their CDS contracts.

The Small Bang Protocol also offers parties a second and final opportunity to adhere to the Big Bang Protocol. By adhering to the Small Bang Protocol, a party that did not adhere to the Big Bang Protocol will be deemed to have adhered to the Big Bang Protocol.

The adherence period for the Small Bang Protocol opened on July 14 and closes on July 24 at 5 p.m. EDT.

A copy of the Small Bang Protocol may be found here.

CFTC

CFTC Requires CTA Registration from SEC-Registered Investment Advisor

On June 25, the Division of Clearing and Intermediary Oversight (DCIO) of the Commodity Futures Trading Commission issued a no-action letter confirming that a person registered as an investment advisor with the Securities and Exchange Commission who offers a managed futures account as part of its portfolio management program would come within the statutory definition of “commodity trading advisor” (CTA) in the Commodity Exchange Act (CEA) and, accordingly, would be required to register as a CTA with the CFTC unless an exemption from registration is available. DCIO concluded that none of the exemptions from CTA registration applied to the presented facts, but noted that the advisor might be able to claim an exemption if its customers do not include collective investment vehicles identified in Section 4m(3) of the CEA.

Read more.

CFTC Allows CPOs to Use IFRS in Lieu of U.S. GAAP

On July 1 and July 8, the Division of Clearing and Intermediary Oversight of the Commodity Futures Trading Commission issued three no-action letters to commodity pool operators (CPOs) of commodity pools operated pursuant to an exemption under CFTC Regulation 4.7 and/or CFTC Regulation 4.13, granting the CPOs relief to use International Financial Reporting Standards in lieu of U.S. generally accepted accounting principles in the preparation of financial reports for the commodity pools. The relief was granted pursuant to CFTC Regulations 140.93 and 4.12(a).

Read CFTC Letter No. 09-28.
Read CFTC Letter No. 09-29.
Read CFTC Letter No. 09-30.

CFTC Addresses Requests for Financial Reporting Relief

On June 26, the Division of Clearing and Intermediary Oversight (DCIO) of the Commodity Futures Trading Commission issued two no-action letters in response to requests from commodity pool operators (CPOs) for relief in connection with financial reporting requirements. The first letter denied the CPO’s request to extend beyond June 29 the deadline for filing the commodity pools’ 2008 annual reports. DCIO stated that the interests of pool participants in receiving timely information outweighed the CPO’s hardship in obtaining financial statements from investee pools. The second letter granted the CPO’s request for stub period relief due to liquidation of the commodity pool’s feeder funds, and allowed the CPO to file an 18-month (instead of a 12-month) report.

Read CFTC Letter No. 09-32.
Read CFTC Letter No. 09-33.

INVESTMENT COMPANIES AND INVESTMENT ADVISORS

Administration Bill Would Require Managers of Hedge and Other Private Funds to Register as Investment Advisors

On July 15, the Obama Administration announced proposed legislation entitled the "Private Fund Investment Advisers Registration Act of 2009" that would amend the Investment Advisers Act of 1940 in a number of ways with the effect of, among other things, requiring all U.S.-based investment advisors with more than $30 million in assets under management to register with the Securities and Exchange Commission. This would affect managers of hedge funds, private equity funds and venture capital funds and many foreign fund managers currently exempt from SEC registration.

Read the Katten *Client Advisory* with more information on the proposed legislation.

BANKING

Federal Agencies Release Final Rules and Guidelines Regarding Accurate Consumer Reporting

On July 2, the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Office of Thrift Supervision, the National Credit Union Administration and the Federal Trade Commission (the Agencies) released final rules and guidelines to promote the accuracy and integrity of information furnished to credit bureaus and other consumer reporting agencies. The rules and guidelines implement the accuracy and integrity and direct dispute provisions in Section 312 of the Fair and Accurate Credit Transactions Act of 2003.

Pursuant to the rules, furnishers of consumer information to consumer reporting agencies must establish and implement reasonable written policies and procedures regarding the accuracy and integrity of consumer information provided to a consumer reporting agency. The guidelines set forth objectives that should be considered by furnishers as they develop such policies and procedures.

In addition, on the same date, the Agencies released an advance notice of proposed rulemaking with respect to the development of a possible proposed addition to the furnisher accuracy and integrity guidelines described above. The specific item for which the Agencies seek information involves whether it would be appropriate for the Agencies to propose an addition to one of the guidelines that would delineate the circumstances under which a furnisher would be expected to provide an account opening date to a consumer reporting agency to promote the integrity of the information. The Agencies also request comment as to whether furnishers should be expected to provide any other types of information to a consumer reporting agency in order to promote integrity. Comments with respect to these issues must be submitted by August 31.

For more information, click here.

STRUCTURED FINANCE AND SECURITIZATION

New York Fed Announces $669 Million of TALF Loan Request for Legacy CMBS

The Federal Reserve Bank of New York announced that on July 16, the first loan subscription date for legacy commercial mortgage-backed securities (CMBS), there were approximately $669 million in loan requests for legacy CMBS under its Term Asset-Backed Securities Loan Facility (TALF). July 16 was also the second loan subscription date for newly issued CMBS, but, as expected, there were no TALF-eligible newly issued CMBS available for purchase, and no newly issued CMBS loan requests were made.

For more information, click here.

ANTITRUST

Delta Air Lines and Virgin Blue Seek Antitrust Immunity

Delta Air Lines and Virgin Blue Airline Group are seeking antitrust immunity from U.S. regulators for a period of five years as a condition to their moving forward with a joint venture related to flights in Australia and the South Pacific. The airlines announced the proposed joint venture on July 8, but Delta has stated that it will not complete the joint venture without antitrust immunity. The joint venture would allow the companies to engage in code-sharing and joint marketing of their routes.

The parties have applied to the Department of Transportation, which has the power to provide airlines under its jurisdiction with antitrust immunity. The application is likely to be controversial because the Department of Justice has criticized the Department of Transportation's review of immunity applications and is likely to insist on an in-depth vetting of the proposed joint venture. Although the request for antitrust immunity is somewhat unusual, it is not wholly unexpected when considered in the context of the Department of Justice's recent increased scrutiny of the airline industry.

Read more.

ERISA

Employee Benefit Plans Must Assess FBAR Filing Requirement for Offshore Accounts

Administrators of employee benefit plans may previously not have been aware of their possible obligation to make "FBAR" filings with the Internal Revenue Service. All U.S. persons with a financial interest in, or signature or other authority over, foreign financial accounts with an aggregate value over $10,000 in a calendar year must file Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts (FBAR).

Recently, the IRS broadened the definition of the "U.S. persons" to whom the FBAR requirements apply and made some other changes to the FBAR form. The publicity about these changes has also focused more attention on the FBAR filing requirement itself.

Employee benefit plans may be subject to the FBAR requirement under circumstances involving investments such as the following:

- A private equity, real estate or hedge fund that is organized outside the U.S.
- An offshore "feeder" fund that invests in a "master" fund
- A securities or futures trading account maintained for the plan in a foreign jurisdiction

The FBAR normally is due June 30 of the year following the calendar year for which it is filed. For 2008 FBARs, the IRS has announced that taxpayers who have recently learned of the FBAR requirement have until September 23 to file. Separately, the IRS has announced that FBARs for pre-2008 calendar years may be filed without penalty by September 23, provided that the taxpayer reported and paid any tax due with respect to the foreign account.

Further information about FBAR filing requirements appears in Katten *Client Advisories* from June 25, June 16 and May 12.

The appropriate persons involved in plan administration should consider whether a plan and/or individuals involved in the administration of the plan may be subject to the FBAR filing requirements for 2008 or prior calendar years, and consult with tax advisors to determine if any action is necessary.

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