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Katten Muchin Rosenman LLP

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SEC/Corporate

SEC Adopts Final Rules for Executive Compensation Disclosure Requirements

On July 26, the Securities and Exchange Commission voted to adopt final rules governing the disclosure of executive and director compensation, related person transactions, and director independence and other corporate governance matters. The changes reflected in the new rules will affect disclosure in proxy statements, annual reports and registration statements, as well as the current reporting of compensation arrangements, and require that most of these disclosures be in plain English. SEC Chairman Christopher Cox declared "The better information that both shareholders and boards of directors will get as a result of these new rules will help them make better decisions about the appropriate amount to pay the men and women entrusted with running their companies."

The final rules are substantially the same as the proposed rules, except for the addition of disclosures concerning the issuance of stock options and changes to the so-called "Katie Couric rule" calling for disclosures of the compensation of up to three additional persons who would not otherwise be included in the Summary Compensation Table, which will be re-proposed for additional comment.

Executive and Director Compensation.

- A new narrative section, Compensation Discussion and Analysis, will discuss the objectives and implementation of executive compensation programs, focusing on the most important factors underlying each company's compensation policies and decisions. The final rule maintains the requirement that the CD&A be filed (not furnished) and thus a part of the disclosure certified by a company's principal executive officer and principal financial officer. The final rule adds a compensation committee report that will be furnished and requires a statement of whether the compensation committee has reviewed and discussed the CD&A with management and recommended its inclusion in the Form 10-K and proxy statement. The final rule also calls for the retention of the Performance Graph.

- A reorganized Summary Compensation Table showing compensation of the principal executive officer, principal financial officer and the three highest paid executive officers for the past three years will include:
  - a dollar value for all equity-based awards, measured at grant date fair value pursuant to Statement of Financial Accounting Standards No. 123(R);
  - a column reporting the amount of compensation under non-equity incentive plans;

- a column reporting the annual change in the actuarial present value of accumulated pension benefits and above-market or preferential earnings on nonqualified deferred compensation;
- a column showing the aggregate amount of all other compensation not reported in the other columns of the table, including perquisites (perquisites will be included in the table unless the aggregate amount is less than $10,000, and interpretive guidance will be provided for determining what is a perquisite); and
- a column reporting total compensation.

- The Summary Compensation Table will be accompanied by two supplemental tables reporting outstanding equity interests.
  - The Outstanding Equity Awards at Fiscal-Year End Table will show outstanding awards representing potential amounts that may be received in the future.
  - The Option Exercises and Stock Vested Table will show amounts realized on equity compensation during the last fiscal year.

- In addition, Tables and disclosure regarding retirement, deferred compensation and post-employment arrangements will include:
  - the Pension Benefits Table, which requires disclosure of the actuarial present value of each named executive officer's accumulated benefit under each pension plan;
  - the Nonqualified Deferred Compensation Table, which requires disclosure with respect to nonqualified deferred compensation plans of executive contributions, company contributions, withdrawals, all earnings for the year and the year-end balance; and
  - a narrative description of any arrangement that provides for payments or benefits payable on termination or a change in control of the company, including quantification of these potential payments.

- A Director Compensation Table (along with a related narrative), similar in format to the Summary Compensation Table, will also be required.

Disclosure Regarding Option Grants. In the final release, the SEC will provide additional guidance regarding disclosure of company programs, plans and practices relating to the granting of options, including in particular the timing of option grants in coordination with the release of material nonpublic information and the selection of exercise prices that differ from the underlying stock's price on the grant date.

The tabular disclosure called for in the proposing release was increased to include disclosure of the date of the action to grant the award if that date is different than the grant date.

The final rule will also require enhanced narrative disclosure about option grants to executives in the CD&A, where companies will be required to discuss information such as the reason a company selects particular grant dates for awards or the methods used to select terms of the awards such as exercise prices. Companies will also be required to answer specific questions about timing of option grants and their relationship to the release of material nonpublic information.

Miscellaneous. The final rules adopted the changes in the proposing release to disclosures regarding related person transactions (increasing the dollar threshold requiring disclosure from $60,000 to $120,000), director independence and other governance matters and Form 8-K disclosures concerning employment arrangements, in most cases without further substantive changes.

Compliance. Compliance with these provisions will be required as follows.

- For Forms 8-K, 60 days or more after publication in the Federal Register;
- For Forms 10-K and 10-KSB, for fiscal years ending on or after December 15, 2006; and
- For proxy and information statements, Securities Act registration statements and Exchange Act registration statements filed on or after December 15, 2006, that are required to include Item 402 and 404 disclosure for fiscal years ending on or after December 15, 2006.

Katten Muchin Rosenman LLP will distribute a Client Advisory after the full text of the release is published by the SEC. The SEC's press release is available at http://www.sec.gov/news/press/2006/2006-123.htm.

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Broker Dealer

Effectiveness of SEC Soft Dollar Interpretation

The Securities and Exchange Commission's most recent interpretation of permitted brokerage and research services that can be paid for with "soft dollars" under the safe harbor of Section 28(e) of the Securities Exchange Act of 1934 (Exchange Act) was printed in the Federal Register on July 24, 2006. The interpretation is effective on publication, but parties may rely upon previous SEC interpretations until January 24, 2007. In other words, research or brokerage services previously permitted but not allowed under the interpretation, such as mass-marketed publications, may continue to be paid for using "soft dollars" until January 24. Other services not clearly within the previous interpretation or the most recent interpretation may now be subject to the scrutiny called for by the new interpretation, i.e., that a good or service is permitted research or brokerage, an affirmative determination by the money manager that it provides the manager lawful assistance and that the commissions paid are reasonable.
http://a257.g.akamaitech.net/7/257/2422/01jan20061800/edocket.access.gpo.gov/2006/pdf/06-6410.pdf

SEC Proposes Amendment to Regulation SHO

Regulation SHO under the Securities Exchange Act of 1934 regulates short sales of securities listed on a national securities exchange. The Securities and Exchange Commission has proposed two amendments. The first would remove the exception for positions established prior to the effective date of Regulation SHO or the date when the security became a threshold security from the requirement that a threshold security with fails to deliver outstanding at a registered clearing agency more than 13 consecutive trading days be bought in. A threshold security is any security of an issuer required to file reports under Section 12 or Section 15 of the Exchange Act relative to which there are fails to deliver at a registered clearing agency over five consecutive settlement days of 10,000 shares or more and equal to at least 0.5% of the total shares outstanding. The second proposal is to eliminate the exception from the buy-in requirement for fails to deliver in a threshold security attributed to short sales by a registered options market maker.
http://www.sec.gov/rules/proposed/2006/34-54154.pdf

Amex Proposes Hybrid Market

The Securities and Exchange Commission has published for comment a proposal by the American Stock Exchange LLC to establish a hybrid market for equity securities, equity like securities and exchange traded funds listed for trading on the Amex. Amex specialists and Registered Traders would be able to stream quotes to the Auction & Electronic Market Integration (AEMI) from proprietary systems, generate quotes based upon parameters in AEMI or enter quotes physically from a "front-end" device supplied by the Amex. They also would be permitted to enter quotes in up to five levels. Floor brokers would be able to enter orders into AEMI or execute the order on the floor. Amex member firms would be able to enter quotes directly into AEMI or through a floor broker. Certain orders, such as "not held" and Rule 144 trades, could not be entered into AEMI. Also, AEMI would not be available when there is excessive volatility, during which time the auction market would be used to reduce volatility and fluctuations in the market.
http://a257.g.akamaitech.net/7/257/2422/01jan20061800/edocket.access.gpo.gov/2006/pdf/06-6357.pdf

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Banking

FDIC Imposes Moratorium on Industrial Loan Company Applications

Today the Board of Directors of the Federal Deposit Insurance Corporation (FDIC) approved a six-month moratorium on applications for deposit insurance by Industrial Loan Companies (ILCs), as well as on notices of change in bank control for existing ILCs. The FDIC will not make any final decisions or accept any future applications for deposit insurance or notices of change in control for ILCs during this period.

The FDIC stated that, "recently, the growth of the ILC industry, the trend toward commercial company ownership of ILCs and the nature of some ILC business models have raised questions about the risks of ILCs to the deposit insurance fund, and whether their commercial relationships pose any safety and soundness risks."

The FDIC explained that it put the moratorium in place to provide time to assess developments in the ILC industry, to determine if any emerging safety and soundness or policy issues exist involving ILCs, and to evaluate whether statutory, regulatory or policy changes need to be made in the oversight of these charters. The moratorium also allows the agency time to further evaluate the various issues, facts and arguments raised in connection with the ILC industry, and to assess whether statutory or regulatory changes or revised standards and procedures for ILC applications and supervision are needed to protect the deposit insurance fund.

The moratorium provides a limited exception only in the unlikely circumstances in which there is a risk to an FDIC-insured institution or to the insurance fund, or if the mission of the FDIC is impaired. The moratorium expires on January 31, 2007.

Currently, 61 ILCs operate in seven states. There are nine ILC applications for deposit insurance and five notices of change in control for existing ILCs pending before the FDIC. All of those applications and notices are subject to the moratorium.
http://www.fdic.gov/news/news/press/2006/pr06073a.html

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Litigation

Scope of Arbitration Clause Determined by Arbitrators, Not by Court

Defendant moved to stay an action seeking specific performance of an agreement in favor of arbitration of the parties' dispute. In opposition, plaintiff argued that the court itself should first determine whether the dispute was subject to arbitration because, absent an express provision to the contrary, courts, not arbitrators, determine the scope of arbitration provisions. In granting defendant's motion, the Court noted that, under the agreement at issue, arbitration between the parties was governed by the American Arbitration Association Commercial Arbitration rules in effect at the time the dispute arose and, as applicable here, those rules expressly conferred upon the arbitrators themselves the authority to determine the scope of the arbitration provision. (*Southern Farms Ltd. v. American Farmland Investors Corp., (2006 WL 2038532 (M.D. Fla. July 19, 2006*)).

Good Faith of Breaching Party May Affect Enforceability of Damages Cap

Lion's Gate alleged that as a result of KFI's breach of a loan agreement, Lion's Gate could not close on a real estate transaction. Relying on a limitations of damages clause in the loan agreement, KFI argued that Lion's Gate's right to recover was limited to amounts it had paid into escrow as part of a commitment fee. Although the Court agreed that, as a general principle, it was appropriate to enforce a contractual cap on damages, that principle did not apply where the breaching party acted in bad faith or with tortious intent. Because Lion's Gate alleged that KFI breached its duty of good faith and acted fraudulently, the Court "decline[d] to decide at this time whether the limitation of damages clause in the contract may be enforced." (*Kennedy Funding, Inc. v. Lion's Gate Development LLC, 2006 WL 2038496(D. N.J. July 19, 2006*)).

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