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Corporate and Financial Weekly Digest

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SEC/CORPORATE

SEC Publishes Proposed Rule Facilitating Shareholder Director Nominations

As reported in the May 22 edition of *Corporate and Financial Weekly Digest*, on June 10, the Securities and Exchange Commission proposed changes to the federal proxy rules to facilitate the exercise of shareholders' rights under state corporate law to nominate and elect directors.

The SEC has this week published its release regarding these proposed changes. The SEC's proposals provide shareholders with two ways to more effectively exercise their rights to nominate directors. First, the SEC is proposing a new proxy rule (Exchange Act Rule 14a-11) that would, under certain circumstances, require companies to include disclosures about shareholder nominees for directors in the companies' proxy materials proposed by long-term or significant shareholders who are not seeking a change of control. The requirement does not apply to shareholders who are prohibited from nominating a director under state corporate law or under the company's organizational documents. Second, the SEC is proposing an amendment to Exchange Act Rule 14a-8(i)(8) to prevent companies from excluding from their proxy materials shareholder proposals that would amend, or that request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations. These proposals would be required to comply with the proposed Rule 14a-11.

To view the full text of the release, click here.

A more detailed analysis of the proposed SEC rule will be distributed in a Katten *Client Advisory* next week.

Multiple Governmental Developments Affecting Executive Compensation

On June 10, the U.S. Treasury Department and the Securities and Exchange Commission announced multiple developments affecting executive compensation.

- *Executive Compensation Reforms Announced and Legislation Proposed*

  Treasury Secretary Timothy Geithner issued a statement indicating that the executive branch will be considering executive compensation reforms with the end goal of "bringing compensation practices more tightly in line with the interests of shareholders and reinforcing the stability of firms and the financial system." In particular, the administration supports legislation for a non-binding vote on executive compensation and the independence of directors on compensation committees and their committee's consultants.

  To view Secretary Geithner's full statement click here.
  To view the "Say-on-Pay" fact sheet click here.
  To view the Compensation Committee Independent fact sheet click here.

- *Treasury Issues Executive Compensation Rules for TARP Participants*

  The Treasury issued an interim final rule on the executive compensation restrictions imposed on recipients of Troubled Asset Relief Program (TARP) funds by the American Recovery and Reinvestment Act of 2009. Such rule imposes new governance requirements, including the appointment of a "pay czar" to review compensation plans of TARP recipients receiving "exceptional assistance", the prohibition of tax "gross-up" payments, and additional disclosure of perquisites and compensation consultants.

  To view the full text of the interim final rule click here.

- *Chairman Schapiro Issues Statement on Executive Compensation*

  In a press release, SEC Chairman Mary Schapiro announced that the SEC is actively considering a package of new proxy statement disclosure rules which will cause companies to consider how compensation affects risk-taking and corporate health. The proposals that are being considered include greater disclosure regarding (i) how a company and its board manage risks, (ii) a company's overall approach to compensation, (iii) potential compensation consultant conflicts of interests, and (iv) experience and qualifications of director nominees and the leadership structure. While the SEC has not generally served a role in setting pay scales or compensation packages, Chairman Schapiro noted that its role is to protect investors through more complete disclosure and that type of information may impact investors' voting and investment decisions.

  To view the full text of the release, click here.

Additionally, on June 11, SEC Division of Corporation Finance Deputy Director Brian Breheny testified concerning the oversight and regulation of executive compensation before the House Committee on Financial Services. Deputy Director Breheny provided testimony on the SEC's efforts to strengthen the disclosure rules so investors have the information they need to make informed decisions.

To view the full text of Deputy Director Breheny's testimony, click here.
To view a more detailed discussion of these compensation developments, please see the June 11, 2009, Katten *Client Advisory*.

LITIGATION

District Court Grants Motion to Dismiss False Projections Claims

A District Court dismissed class action claims asserted under Section 10(b) and 20(a) of the Securities Exchange Act of 1934. Plaintiffs, investors in a retail clothing chain, alleged that defendants made material misstatements or omissions in two press releases that included financial projections that the defendant corporation failed to meet. Defendants asserted that plaintiffs failed to meet the heightened pleading requirements of Federal Rule of Civil Procedure 9(b) as well as the Private Securities Litigation Reform Act of 1995 (PSLRA).

The Court found that plaintiffs failed to allege scienter. The Court stated that, if a statement is "forward-looking" and is accompanied by sufficient cautionary language, it is protected. If the statement does not have the requisite cautionary language, the plaintiff must show that the defendants had actual knowledge of their false or misleading nature in order to allege scienter. Finally, if the statements are not forward-looking, the plaintiff must show that the defendants made the statements recklessly. The Court found that to the extent that the alleged misstatements were forward-looking projections, plaintiffs did not adequately allege that defendants had actual knowledge of their falsity. Additionally, to the extent that the statements related to present or historical facts, plaintiffs may have alleged that the defendants acted negligently in making such statements, but failed to allege that defendants were reckless in making such statements. Therefore, because plaintiffs had failed to allege scienter as required under the PSLRA, the court dismissed the complaint with prejudice. (*Gruhn v. Tween Brands, Inc.*, 2009 WL 1542798 (S.D. Ohio June 2, 2009))

District Court Denies Summary Judgment on Alter Ego Claim

A District Court denied a motion for summary judgment claiming that related defendant corporations were alter egos. Defendant PSNet agreed to purchase 70% of the equity in the plaintiff corporation for $10 million. When PSNet failed to fund the transaction, plaintiffs sued and asserted that PSNet, which was created to find investments for PSNet Communications, was a mere alter ego of PSNet Communications and sought summary judgment against PSNet Communications.

Plaintiffs argued that PSNet never had any capital, revenue, insurance or employees and never did any business other than a single failed real estate transaction and the transaction at issue. In rejecting this argument, the Court found that plaintiffs had failed to demonstrate that PSNet had intermingled funds or that PSNet Communications had failed to respect the corporate form of PSNet. The Court therefore held that, while PSNet might have been an undercapitalized start-up company, it could not find as a matter of law that it was a mere alter ego of the cell phone company. Therefore, the court held that this was an "intensely fact-driven inquiry" and denied plaintiffs' summary judgment motion. (*Needa Parts Mfg., Inc. v. PSNet, Inc.*, 2009 WL 1543390 (E.D. Mich June 2, 2009))

BROKER DEALER

FINRA CEO Addresses Oversight of Investment Advisors

Richard Ketchum, chairman and chief executive officer of the Financial Industry Regulatory Authority, delivered a speech at the National Association for Variable Annuities Government and Regulatory Affairs Conference on June 8 in which he stated that if FINRA had the authority to regulate investment advisors, investor protection would be improved. Ketchum said FINRA is "uniquely positioned to build an oversight program for investment advisors quickly and efficiently." Ketchum also noted the "disparity" between oversight regimes for investment advisors and broker-dealers, particularly between the fiduciary standard for investment advisors and the rule requirements for broker-dealers (including suitability). Accordingly, he stated that holding investment advisors and broker-dealers to two different fiduciary standards was "untenable," and that FINRA, in its effort to reform the financial regulatory system, will consider the need to explore seriously whether a properly designed fiduciary standard can effectively be applied to broker-dealer selling activities. Ketchum also discussed regulatory and oversight issues with respect to the annuities industry.

Click here to read the speech.

SEC Approves Amendments Expanding Definition of "TRACE-Eligible Security"

On April 14, the Securities and Exchange Commission approved amendments to the definition of "TRACE-eligible security" contained in Financial Industry Regulatory Authority Rule 6710(a). The amendments broaden the definition of TRACE-eligible security by deleting the requirements that, to be TRACE-eligible, a security must: (i) be registered under the Securities Act of 1933, as amended (Securities Act) or (ii) if resold under Rule 144A of the Securities Act, initially offered and sold under the exemption from registration in Section 4(2) thereof. The amended definition provides that if a security is a "restricted security" as defined in Securities Act Rule 144(a)(3), it is TRACE-eligible if sold pursuant to Securities Act Rule 144A. The amendments, effective on June 15, are aimed at extending price transparency to corporate bonds that are being purchased and sold by diverse market participants, including retail investors, and enhancing the surveillance of the corporate bond market.

FINRA Regulatory Notice 09-24 is available here.

BANKING

Federal Agencies Release FAQs on Identity Theft Red Flags and Address Discrepancies

On June 11, the staff of the Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, National Credit Union Administration, Office of the Comptroller of the Currency, Office of Thrift Supervision and the Federal Trade Commission (FTC) (collectively, the Agencies) released frequently asked questions (FAQs) to assist financial institutions, creditors, users of consumer reports, and card issuers in complying with the final rulemaking on Identity Theft Red Flags and Address Discrepancies implementing Section 114 of the Fair and Accurate Credit Transactions Act of 2003 (FACT Act) and Section 315 of the FACT Act that amended the Fair Credit Reporting Act.

Many of the questions the Agencies have received are answered in the supplemental information to the final rules. These FAQs elaborate on the supplemental information where additional clarification is necessary and also explain the staff's view of how select provisions of the rulemaking apply to situations that were not specifically addressed in the final rules or supplemental information. The Agencies indicated that staff may supplement or revise these FAQs as necessary or appropriate in light of further questions and experience. The FTC will be issuing additional FAQs to answer questions specific to entities under FTC jurisdiction.

While the three rules themselves do not contain specific record retention requirements, (i) financial institutions and creditors must be able to demonstrate that they have complied with the requirements of the Red Flags and Card Issuers' Rules, and (ii) users of consumer reports must be able to demonstrate that they have complied with the requirements of the Address Discrepancy Rules, in addition to any other applicable record retention requirements.

The Agencies clarified that their information security standards, which help to reduce identity theft ("a fraud committed or attempted using the identifying information of another person without authority") by keeping individuals' sensitive data from falling into the hands of an identity thief, are different that the Red Flags Rules and Guidelines. The information security standards require financial institutions to have reasonable policies and procedures that are designed to safeguard customer information and protect it from unauthorized access or misuse and to ensure the proper disposal of customer and consumer information. By contrast, the Red Flags Rules and Guidelines seek to ensure that financial institutions and creditors are alert for signs or indicators that an identity thief is actively misusing another individual's sensitive data, typically to obtain products or services from the institution or creditor. The Red Flags Rules require financial institutions and creditors that offer or maintain "covered accounts" to have policies and procedures to identify patterns, practices or activities that indicate the possible existence of identity theft; to detect whether identity theft may be occurring in connection with the opening of a covered account or an existing covered account; and to respond appropriately.

Read more.

ANTITRUST

International Competition Network Adopts Merger Review Recommendations

Last week, the International Competition Network (ICN), a group of antitrust enforcement agencies representing nearly 100 different countries, adopted three important new merger review standards. These recommendations are intended to help create uniform merger review analysis across different jurisdictions. ICN adopted these new standards at its eighth annual conference, where 450 delegates representing more than 80 antitrust agencies spent three days in Zurich, Switzerland, discussing ways to facilitate uniform competition enforcement standards.

Specifically, the three recommendations that ICN adopted relate to the methods and tools that enforcement agencies should use when evaluating the competitive effects of a merger. First, ICN recommended that antitrust agencies perform competitive effects analysis to determine whether a potential merger would create or enhance anti-competitive market power. In particular, the ICN urged antitrust authorities to weigh the potential market effects if the merger is consummated as well as if it is not. Second, ICN recommended that antitrust agencies consider unilateral and coordinated effects of horizontal mergers on competition. Finally, ICN recommended that regulators apply both economic theory and real-world evidence to weigh the competitive effects of a proposed merger. These three recommendations will hopefully help create a standardized method of examining mergers.

For more information about ICN or the annual conference, please click here.

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