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Corporate and Financial Weekly Digest

Business/Financial News in Brief
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SEC/Corporate

SEC Announces 17 Companies Have Joined Its Interactive Data Pilot Program

The Securities and Exchange Commission has announced that, to date, 17 issuers (including Bristol-Myers Squibb, Microsoft, Pfizer and Xerox) have agreed to participate in a pilot program to use interactive data in their financial statement filings. The program will enable participants to evaluate the benefits of using interactive data, provide feedback to the SEC, and enable investors and analysts to assess new techniques for analyzing interactive data reports submitted to the SEC in eXtensible Business Reporting Language (XBRL) format. To encourage voluntary participation in the program, the SEC has guaranteed expedited reviews of registration statements and annual reports for participants in the test group. Companies interested in joining the test group should visit the interactive data spotlight page at http://www.sec.gov/spotlight/xbrl.htm or contact Jeffrey Naumann in the SEC's Office of the Chief Accountant (naumannj@sec.gov) or Brigitte Lippmann in the SEC's Division of Corporation Finance (lippmannb@sec.gov) for additional information. http://www.sec.gov/news/press/2006-43.htm

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Banking

Report Issued on Improving Financial Privacy Notices for Consumers

The Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Federal Trade Commission, the National Credit Union Administration, the Office of the Comptroller of the Currency, and the Securities and Exchange Commission have released a report entitled "Evolution of a Prototype Financial Privacy Notice" as part of their ongoing efforts to develop financial privacy notices easier for consumers to read, understand and use. According to the report's findings, survey data indicate that many consumers neither read nor understand the notices that financial institutions provide under regulations previously issued by these agencies in 2000. While there is a general awareness of information sharing practices, most consumers do not understand them and, instead, are overwhelmed by complex information. In the agencies' views, financial privacy notices could include all information required by law in a short, readily understandable document that would enhance consumers' ability to read the notices and make informed choices about the use of their personal information. The six agencies,

together with the Office of Thrift Supervision, will fund a second phase of the project to measure the effectiveness of the prototype and other examples of notices. The agencies have deferred consideration of policy action with respect to financial privacy notices until the second phase of consumer testing is completed.
http://www.ftc.gov/privacy/privacyinitiatives/ftcfinalreport060228.pdf

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Broker Dealer

NSCC Adopts Buy-in Procedures for Non-CNS Fails

The National Securities Clearing Corporation (NSCC) has received Securities and Exchange Commission approval to allow buy-ins through NSCC's continuous net settlement system (CNS) for orders that are outside of CNS. Under SEC Regulation SHO, a firm's aged short sale in a security noticed by a clearing agency must be bought in. NSCC is now allowing a firm receiving a buy-in notice for a non-CNS trade to transmit the notice to NSCC together with the name of the notifying firm. NSCC will put that buy-in in its processing for the next business day for fulfillment as a priority item.
http://a257.g.akamaitech.net/7/257/2422/01jan20061800/edocket.access.gpo.gov/2006/pdf/E6-4433.pdf

NYSE Issues Guidance on Reporting Violations

The New York Stock Exchange, Inc. has issued Information Memorandum 06-11 providing guidance on when a member firm must report on Form RE-3. NYSE Rule 351(a)(1) requires reporting violations of the federal securities laws, the rules of a self-regulatory organization or conduct inconsistent with just and equitable principles of trade or detrimental to the interests or welfare of the NYSE that has been engaged in by an associated person of the member firm or the firm itself. The guidance states that the reporting duty attaches once the firm has concluded that violative conduct has taken place. This duty must be read together with Rule 351(a)(10) which requires reporting of disciplinary action involving a fine or withholding of commissions in excess of $2,500 or other significant limitation on the activities of the affected person. If the firm's response to the violative conduct is less severe than that set forth in Rule 351(a)(10), no report under Rule 351(a)(1) is required. De minimis violative conduct need not be reported unless it is recidivist or ongoing. Where, as a result of violative conduct, a firm terminates a person and reports this on Form U5, an RE-3 filing is not needed. However, if the person is not a registered person, an RE-3 filing is required. Isolated or individual exceptions to otherwise effective and regulatory compliant operations are not the sort of matters that would trigger a reporting obligation. However, systemic failures involving numerous customers, multiple errors or significant dollar amounts should be reported.
http://apps.nyse.com/commdata/PubInfoMemos.nsf/AllPublishedInfoMemosNyseCom/85256FCB005E19E88525712D00543576/$FILE/Microsoft%20Word%20-%20Document%20in%2006-11.pdf

NYSE Guidance on Marketing Market Indexed/Linked Certificates of Deposit

The New York Stock Exchange, Inc. has issued Information Memorandum 06-12 on the marketing of market indexed/linked certificates of deposit. It states that, in general, when marketing a new product, firms have a responsibility to make certain that the product is well understood both by its originators and by it sales force. Firms must also identify the customer criteria that will define the appropriate market for a new product generally and train their personnel to assure they can identify the suitable customers. This involves education of the registered representatives and development of disclosure materials for the

intended customers, as well as establishing internal controls to monitor and supervise the new product's sales and identify any problems that may arise. The NYSE defined market indexed/linked certificates as a zero coupon bond coupled with an option on a market index, both of which have a term of 5 to 7 years. The NYSE stressed disclosure of market risk of the product if sold prior to its maturity, liquidity risk (lack of a ready market), call risk (the bond may be called prior to maturity of the product), the tax implications of including accreted value of the zero coupon bond in income in the year of accretion rather than when finally received, and valuation of the product. The NYSE stated that the customer's account statement must report the product at its then current market value and, unless that is the case, it may not be reported at cost or at termination value. It also stressed the need to train the personnel selling this product.
http://apps.nyse.com/commdata/PubInfoMemos.nsf/AllPublishedInfoMemosNyseCom/85256FCB005E19E8852571330062CAE1/$FILE/Microsoft Word - Document in 06-12.pdf

NASD Proposes to Extend Manning Rule to Non-Market Makers

NASD has filed with the Securities and Exchange Commission a proposal to extend IM-2110-2 to firms that are not market makers that hold a customer limit order. The Manning Rule requires a market maker that receives a customer limit order to execute that order before it may trade as a market maker at the same or better price in that security. The amendment would apply to trades effected between 9:30 a.m. and 6:30 p.m. (EST). Any firm, whether or not a market maker in the security, that trades as principal, other than as a riskless principal, for its own account and at the same time holds a customer limit order, whether from a customer of the firm or a customer of another firm, must execute the customer's limit order before trading for its own account at the limit order price or better. Exceptions include where the firm and customer agree otherwise and either the customer is an institutional investor as defined in NASD Rule 3110(c)(4), or the order is for 100,000 shares or more with a price of at least $100,000. Another exception is where the customer limit order is readily marketable at the time received. However, if the order is not then executed and the market deteriorates, i.e., falls below the limit order price, the Manning Rule will apply.
http://a257.g.akamaitech.net/7/257/2422/01jan20061800/edocket.access.gpo.gov/2006/pdf/E6-4434.pdf

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United Kingdom Developments

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FSA Will Permit Funds of Hedge Funds to be Marketed to Retail Investors

The Financial Services Authority (FSA) has announced a decision in principle to permit funds of hedge funds to be marketed to retail investors. It will consult during the first quarter of 2007 on broadening the range of funds that can be marketed to retail investors to include authorized funds of hedge funds. This will enable retail investors to invest in products with the investment characteristics of hedge funds through products that will be subject to the FSA's regime for authorized collective investment schemes. Some details of the proposed regime have already been indicated, particularly with respect to investor protection. Authorized funds of hedge funds will be subject to structural and operational safeguards including a requirement to have an independent depositary. In addition, their investment powers will be

subject to liquidity criteria in respect of the underlying funds as well as concentration and risk spreading criteria.
http://www.fsa.gov.uk/pages/Library/Communication/PR/2006/027.shtml
http://www.fsa.gov.uk/pubs/discussion/fs06_03.pdf

FSA Sets Out Its Regulatory Priorities for the Asset Management Sector

A March 28th speech by Dan Waters, Asset Management Sector Leader at the Financial Services Authority (FSA), sets out FSA's current regulatory priorities for the Asset Management Sector, including (1) simplification of FSA investment product disclosure at the point of sale; (2) "treating customers fairly" through the value chain -- addressing the fair treatment of customers at any of four stages – product design, marketing and promotion, sales and advice, and after sale care (including complaints handling); and (3) responding to European initiatives - in particular the EU Markets in Financial Instruments Directive (MiFID), due to be fully implemented by November 2007. Issues arising in connection with MiFID include the need for managers to establish and implement best execution arrangements; issues relating to new pre- and post-trade transparency requirements; the introduction of new suitability and appropriateness requirements for dealing customers; and changes to the customer classification regime; and issues with respect to for outsourcing key services – particularly to entities located outside the European Economic Area.

The full text of the speech is available at:
http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2006/0328_dw.shtml

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Litigation

Per Se Rule Applies to Vertical Minimum Price-Fixing Agreements

Plaintiff retailer alleged that defendant manufacturer caused it to suffer an antitrust injury when defendant terminated plaintiff for violating its minimum pricing policy. On appeal from a judgment entered on a jury verdict in favor of plaintiff, defendant challenged application of the per se rule to plaintiff's vertical price-fixing claims, arguing that the rule of reason should have been applied. Affirming the District Court, the Fifth Circuit found that application of the per se rule to vertical minimum price-fixing agreements was consistent with Congressional intent and properly applicable to distribution-termination cases where concerted action is taken to set prices. Plaintiff successfully proved that defendant used coercion to fix prices that, under the per se rule, properly were presumed to have caused plaintiff competitive harm. (*PSKS, Inc. v. Leegin Creative Leather Products*, 2006 WL 690946 (5th Cir. Mar. 20, 2006))

Complaint Failed to Allege that Defendant Breached a Legal Obligation

Plaintiff entered into a one year exclusive distribution agreement with defendant manufacturer that, among other things, provided for renewal of plaintiff's exclusive distributor status if certain conditions and projected unit sales goals were met. Five years later, defendant advised plaintiff that it would no longer have exclusive distributor status. After defendant began to deal directly with plaintiff's customers, plaintiff sued, alleging breach of contract and tortious interference claims. The Third Circuit, affirming dismissal of the complaint, held that plaintiff failed to allege that defendant was under any contractual and/or legal obligation at the time it revoked plaintiff's exclusive distributorship status. Among other

things, the complaint did not set forth facts to support allegations that the agreement had been renewed after the first year. The Court further held that, under Pennsylvania's "gist of the action" doctrine, the essence of plaintiff's claim was contractual and, as a result, plaintiff was precluded from raising tort claims. (*Chemtech International, Inc. v. Chemical Injection Technologies*, Inc., 2006 WL 690837 (3d Cir. Mar. 20, 2006))

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CFTC

FinCEN Extends Effective Date of Rules Requiring Enhanced Due Diligence for Foreign Correspondent Accounts

The U.S. Department of the Treasury's Financial Crimes Enforcement Network (FinCEN) has delayed the effective date of a portion of its rules adopted pursuant to Section 312 of the USA PATRIOT Act. The rules, published in the Federal Register on January 4, 2006, require securities broker-dealers, futures commission merchants, introducing brokers, mutual funds and banks and trust companies to perform due diligence and, in some cases, enhanced due diligence, with regard to accounts established or maintained for "foreign financial institutions." A foreign financial institution includes any foreign organized entity that would be a bank, broker-dealer, futures commission merchant, introducing broker or mutual fund if it were organized and situated in the United States. FinCEN has extended from April 4 to July 5 the date by which U.S. financial institutions must begin to apply the due diligence provisions in the rules for new accounts. The October 2 effective date for existing accounts is unchanged.
http://www.fincen.gov/312_extension_special_due_diligence.pdf

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