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Corporate and Financial Weekly Digest

MAY 8, 2009

SEC/CORPORATE

SEC Filing Fees to Increase Significantly

On April 30, the Securities and Exchange Commission announced that for the government's fiscal year 2010, registration fees under the Securities Act of 1933 will increase from the current rate of $55.80 per million dollars registered to $71.30 per million dollars, an increase of approximately 28%. This increased rate will also be applicable to the repurchase of securities in going-private transactions pursuant to Section 13(e) of the Securities Exchange Act of 1934, as well as to proxy solicitations and statements in corporate control transactions. The fee rate applicable to securities transactions on the exchanges and in certain over-the-counter markets will at the same time decrease from $25.70 per million dollars to $12.70 per million dollars.

These new rates were calculated by the SEC under the Investor and Capital Markets Fee Relief Act that sets dollar targets for statutory fee collections for each fiscal year. The SEC must set rates for fees to levels that it projects will generate collections equal to such targets. For the 2010 fiscal year, these targets increase under the Act.

New rates will be effective on October 1 or five days after the date on which the SEC receives its regular Congressional appropriation, whichever date comes later. The SEC will publicly announce the actual effective date of the new fees. In the past, delays in Congress in passing appropriations bills have resulted in an effective date well beyond October 1.

Read more.

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LITIGATION

Federal Court Holds Scienter Sufficiently Pleaded and Denies Motion to Dismiss Securities Fraud Claims

A federal district court has ruled that plaintiffs in a securities fraud action against an investment fund and its advisors sufficiently pleaded claims under Section 10(b) of the Securities and Exchange Act of 1934 and Rule 10b-5. The action arose out of an investment plaintiffs made in the defendant fund, which was organized to make loans to a property development company pursuant to a revolving line of credit. The property development company subsequently defaulted on the loans, causing the investment fund to sustain losses.

In denying defendants' motion to dismiss, the court held that plaintiffs' allegations concerning the individual defendant's "close familial ties" to the development company, as well as defendants' receipt of a $300,000 placement fee, were sufficient to demonstrate a strong inference of scienter. Analyzing the complaint's allegations under the Supreme Court's decision in *Tellabs, Inc. v. Makor Issues and Rights, Ltd.*, 551 U.S. 308 (2007), the court found that the inference that the individual defendant knew of the precarious financial condition of the property development company at the time he solicited plaintiffs to invest was at least as compelling as any other inference that could be drawn.

In addition, the court held that even if the allegations concerning the individual defendant's familial ties and the placement fees defendants received did not give rise to a strong inference of scienter, plaintiffs' allegations that

defendants failed to do "any" due diligence with respect to the property development company prior to recommending the investment to plaintiffs were adequate to plead scienter. In support of their allegations, plaintiffs cited a letter in which defendants boasted "of a 'high level' of collateral" with respect to the loans, when, it was revealed just a few months later, that there was, in fact, "no collateral." The court held that, under the circumstances, the alleged lack of collateral alone gave rise to a strong inference of scienter. (*Kahn v. Ran*, 2009 WL 1138504 (E.D. Mich. Apr. 27, 2009))

Third Circuit Affirms in Part Dismissal of Securities Action Based on Forward-Looking Statements

The Third Circuit Court of Appeals affirmed in part the dismissal of a shareholder class action against Avaya, Inc. and two of its officers, holding that certain of defendants' allegedly false statements were forward-looking and therefore protected by the Private Securities Litigation Reform Act's (PSLRA's) safe-harbor provisions. Plaintiffs had alleged that defendants made numerous misleading statements in violation of the Securities and Exchange Act of 1934, including statements about Avaya's growth potential.

The Third Circuit rejected plaintiffs' claim that defendants' statements that the company was "on track" to meet its goals—which later turned out to be incorrect—were present statements of fact that could form the basis for a securities fraud claim. Instead, the court held that these statements, particularly when viewed in the context of the future projections of which they were a part, were entitled to protection under the PSLRA's safe-harbor provision. In addition, because the statements were covered by the safe-harbor provision, in order to be actionable, plaintiffs were required to demonstrate that they were made with actual knowledge of their falsity, which they had not done. As a result, the court affirmed the dismissal of all claims based upon the statements that the company was "on track" to meet its financial goals. (*Institutional Investors Group v. Avaya, Inc.*, 2009 WL 1151943 (3d Cir. Apr. 30, 2009))

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BROKER DEALER

NYSE Implements Interim Procedures for Incompatible Orders

On April 30, NYSE Regulation, Inc. issued Information Memo 09-19 to set forth interim procedures for members and member organizations handling two-sided block trades greater than 6.5 million shares, which are currently incompatible for entry into the New York Stock Exchange order management systems (i.e., NYSE BBSS). The NYSE is planning on implementing systems changes to its order management systems to accommodate larger orders. Until these changes take place, members and member organizations must follow certain interim procedures with respect to two-sided block orders greater than 6.5 million shares, such as creating a paper order ticket immediately upon receiving such an order (containing all elements required under Securities and Exchange Commission and NYSE rules regarding the terms of the order) and entering such orders into the NYSE's Front-End Systemic Capture database on an "as of" basis immediately following the reporting of the block transaction.

To read NYSE Regulation Information Memo 09-19, click here.

NYSE Adds Temporary Rule Suspension for Extreme Order Imbalance at Close

The New York Stock Exchange, LLC and NYSE Amex, LLC (collectively, the Exchanges) have amended Rule 123C to provide the Exchanges with the ability to temporarily suspend certain rule requirements relating to closing of securities at the Exchanges. In October 2008, the NYSE amended Rule 48 to include the close of trading at a time when a qualified Exchange officer would be permitted to declare an extreme market volatility condition, which would allow the Exchanges to temporarily suspend certain rules. As set forth in Information Memo 09-20, the Exchanges have now deleted these provisions from Rule 48 and moved them to Rule 123C, some on a permanent basis and some on a pilot basis.

As part of the amendments to Rule 123C, pilot Rule 123C(8)(a)(1) provides that the Exchanges may temporarily suspend Rule 52 (which relates to hours of operation) on a security-by-security basis so that interest may be solicited—including interest that may not have been present prior to 4:00 p.m.—to offset any imbalance that may exist as of 4:00 p.m. (or earlier, in the case of an earlier scheduled close). In addition, under Rule 123C(8)(a)(2), the Exchanges may temporarily suspend the restriction on canceling a market-on-close or limit-on-close order that

is a legitimate error after 3:50 p.m. on an order-by-order basis if such an erroneous order would cause significant price dislocation at the close. Procedurally, only the NYSE Designated Market Maker in a particular security may request the relief available under these amendments and must satisfy certain supervisory, approval and record-keeping requirements when doing so.

Please click here to read NYSE Regulation Information Memo 09-20.

CBOE Seeks to Amend Margin Requirements for Vested Employee Options

The Chicago Board Options Exchange, Inc. (CBOE) is seeking comments on its proposed rule change to amend its margin requirements in an effort to facilitate the ability of account holders to use vested and currently exercisable compensatory employee stock options (Vested Employee Options) issued by publicly traded companies as collateral for writing call options that have the same underlying security as the Vested Employee Option. Specifically, the proposal would allow account holders to sell listed equity call options on the same security that underlies their Vested Employee Options without posting margin. Given the uncertificated nature of employee stock options, the proposal contains certain requirements in order to secure the account holder's obligations in such transactions. An amendment to the original proposed rule change provides that publicly traded companies issuing Vested Employee Options will maintain that such options are covered by an effective registration statement on Form S-8 and will notify the broker-dealer immediately if the registration statement becomes ineffective.

The proposed rule change is available here.

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CFTC

CFTC Proposes Revised Adjusted Net Capital Requirements for FCMs and IBs

The Commodity Futures Trading Commission has proposed amendments to the minimum adjusted net capital requirements for futures commission merchants (FCMs) and introducing brokers (IBs). Under the CFTC's proposed amendments, the minimum dollar amount of adjusted net capital would be raised to $1 million for an FCM and $45,000 for an IB. The proposal also would include customer and noncustomer positions in cleared over-the-counter (OTC) derivative instruments (whether cleared in the U.S. or abroad) in the calculation of an FCM's "risk-based" adjusted net capital requirement, and would require FCMs to take charges to their regulatory capital ("haircuts") for cleared OTC positions that are carried in proprietary accounts in a manner comparable to those that are required for exchange-traded futures and options. In addition, the proposal would increase the risk margin requirement for both customer and noncustomer positions to 10% (from 8% and 4%, respectively).

In the same proposal, the CFTC has requested comment on the advisability of increasing the CFTC's adjusted net capital requirements for FCMs that are also securities broker-dealers to include, in addition to the amount that would otherwise be required by CFTC rules, an amount equal to such broker-dealer/FCM's net capital requirement under Securities and Exchange Commission Regulation 15c3-1. Currently, CFTC and SEC regulations each require a dually registered firm to maintain net capital in excess of the higher of the two capital requirements. If the CFTC were to move forward, a dually registered firm's requirement would be the sum of the two requirements.

The comment period for the proposal closes on July 6.

Read more.

NFA Extends Effective Date for Portions of NFA Compliance Rule 2-43(b)

The National Futures Association (NFA) has extended the effective date for portions of its new Compliance Rule 2-43(b), which prohibits forex dealer members (FDMs) from allowing customers to carry offsetting positions and generally requires an FDM to offset positions in a customer account on a first-in, first-out (FIFO) basis. The rule was originally scheduled to become effective for any positions established after May 15, but due to concerns raised by FDMs about the time needed to comply with the FIFO portion of the rule, NFA has postponed the effective date for that portion of the rule until July 31. The effective date for the remainder of the rule remains May 15.

Read more.

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BANKING

FDIC Announces Expansion of Ombudsman's Office to Assist Customers With Loans at Failed Banks

The Federal Deposit Insurance Corporation (FDIC) on May 5 announced the creation of a new unit within the FDIC's Office of the Ombudsman specifically designed to assist customers with loans at failed banks. The FDIC's Division of Resolutions and Receiverships (DRR) will continue to have primary responsibility for working with customers of failed banks to address their concerns and transition them to new banking and lending relationships. This new unit will give borrowers an additional venue for having their concerns addressed by the FDIC. The FDIC Office of the Ombudsman has a nationwide presence in each of the agency's six regions and helped resolve more than 1,100 cases in 2008. The FDIC stated that "[a]s the pace of failures increases, additional staffing in the office will help provide service and clear communication between all parties."

The FDIC has also produced "A Borrower's Guide to an FDIC Insured Bank Failure." This guide will help inform customers that had loans with failed institutions about what they can expect to occur in the receivership process, including the disposition of loans, workout steps taken on delinquent loans and an explanation of borrower rights.

Read more.

Banking Agencies Release Results of "Stress Tests"

On May 7, the Board of Governors of the Federal Reserve System (Federal Reserve) released the results of its comprehensive assessment of the country's 19 largest bank holding companies. The supervisory capital assessments (SCAPs) were conducted collaboratively by the Federal Reserve, the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation (collectively, the Banking Agencies).

The intent of the stress tests was to determine whether these bank holding companies had a sufficient "capital buffer" to withstand losses and sustain lending even if the economic downturn is more severe than currently anticipated.

According to the SCAPs, 10 of the 19 bank holding companies surveyed will need to raise a total of $74.6 billion in capital. In total, the Banking Agencies estimated that losses could reach $599 billion for the group in 2009 and 2010, with most of the losses coming from residential mortgages and other consumer loans. Bank holding companies that need to supplement their capital as a result of the SCAP program will have one month to design a plan, subject to supervisory approval, to put the SCAP capital buffer in place, and the plan must be implemented by early November 2009.

The SCAPs were complementary to the U.S. Treasury Department's Capital Assistance Program, which provides capital to financial institutions as a "bridge to private capital in the future."

For more information, click here.

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STRUCTURED FINANCE AND SECURITIZATION

FRBNY Announces $10.6 Billion of TALF Loan Requests in May

On May 5, the Federal Reserve Bank of New York announced that on the May subscription date prospective borrowers requested $10.6 billion in TALF loans. That marks a significant increase from the April subscription, for which there were only $1.7 billion in TALF loan requests.

The types of asset-backed securities (ABS) collateralizing the loan requests also increased. In April, the loan requests were limited to $811 million of auto ABS and $896 million of credit card ABS. In May, however, there were loan requests related to $2.1 billion of auto ABS, $5.5 billion of credit card ABS, $2.3 billion of student loan ABS, $456 million of equipment ABS and $86 million of Small Business Administration loan ABS.

Read more.

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ANTITRUST

FTC Investigating Overlap On Google and Apple Boards

On May 4, it was reported that the Federal Trade Commission is investigating whether having two common directors on the boards of Apple Inc. and Google Inc. violates antitrust law. The statute at issue is Section 8 of the Clayton Act, 15 U.S.C. Section 19, known as the prohibition on "interlocking directorates." It prohibits anyone from serving as a director or officer in any two corporations that are "by virtue of their business and location of operation, competitors, so that the elimination of competition by agreement between them would constitute a violation of any of the antitrust laws." The prohibition does not apply if one corporation's revenue from the products on which they compete is less than two percent of its annual revenue.

In other words, if the two corporations *could* reach an illegal agreement not to compete with each other in selling specific products or services, then those corporations may not share common directors. In the case of Apple and Google, both companies compete in the smartphone and smartphone operating system markets—Apple with the iPhone and iPhone OS, and Google with the G1 phone and its Android platform. The companies also compete in the web browser market (Apple's Safari and Google's Chrome) and in the video and music distribution markets (Apple's iTunes and the Google-owned YouTube).

The government has rarely challenged interlocking directorates in the past. But the challenges it has brought typically result in a director stepping down, rather than a protracted legal battle. The current FTC challenge reminds businesses who share directors to be sensitive to whether they are potential competitors who offer any of the same products or services.

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EU DEVELOPMENTS

Proposed Alternative Investment Fund Managers Directive Published

Last week we reported that on April 29, the European Commission had announced a proposed Alternative Investment Fund Managers Directive (Proposed Directive) and that the Proposed Directive had not yet been published by the Commission.

The Proposed Directive has now been published and is available here.
See also the Katten *Client Advisory* on this subject.

Commission Publishes Two Recommendations on Remuneration

Last week we reported that on April 29, the European Commission had announced two Recommendations on remuneration: a Recommendation on remuneration in the financial services sector (FS Remuneration Recommendation) and a Recommendation on the regime for the remuneration of directors of listed companies (Directors' Pay Recommendation) and that the Commission had only published press releases and frequently asked questions (FAQs) in relation to the two Recommendations.

Both Recommendations have now been published.

The FS Remuneration Recommendation is available here.
The Directors' Pay Recommendation is available here.

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