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CORPORATE & FINANCIAL
WEEKLY DIGEST

November 11, 2011

SEC/CORPORATE

House Approves Bills Providing Crowdfunding and Solicitation Exemptions

On November 3 the U.S. House of Representatives passed H.R. 2930 (the “Entrepreneur Access to Capital Act”) and H.R. 2940 (the “Access to Capital for Job Creators Act”).

H.R. 2930, the “crowdfunding” bill, would amend the Securities Act of 1933 (the Act) to add new Sections 4(6) and 4A which would exempt from the registration requirements of Section 5 of the Act transactions where the aggregate amount of securities sold by an issuer in a 12 month period does not exceed (a) $1,000,000 or (b) $2,000,000 if the issuer provides potential investors with audited financial statements. However, an offering would not qualify for the foregoing exemption if the amount sold to any individual investor in reliance on the exemption exceeds the lesser of (i) $10,000 and (ii) 10% of such investor’s annual income. Securities sold pursuant to the exemption may not be resold for one year unless such securities are sold to the issuer or to an “accredited investor”, as defined in Rule 501(a) under the Act.

H.R. 2930 would also establish requirements for intermediaries and issuers who rely on the newly created exemption. Intermediaries, or issuers who do not utilize intermediaries, are required, among other things, to: (a) warn investors of (i) the speculative nature of the investment and (ii) the restrictions on sales of the securities, (b) take measures to reduce the risk of fraud with regards to the transaction, (d) provide the Securities and Exchange Commission with the name, address, website address and employees of the intermediary or issuer, as applicable, (e) provide the SEC with investor level access to the intermediary’s or issuer’s, as applicable, website, (f) require each potential investor to answer questions that demonstrate an understanding of the level of risk applicable to investments in small issuers and the risks of illiquidity, (g) state a target offering amount and deadline and provide for a third party custodian to withhold proceeds until the aggregate capital raised is no less than 60% of the target amount, (h) carry out a background check on the issuer’s principals, (i) provide the SEC and potential investors with notice of the offering and specified other information not later than the first day securities are offered to potential investors, (j) outsource cash-management functions to a qualified third party custodian and (k) provide the SEC with a notice upon completion of the offering. Issuers who do not utilize intermediaries are not required to satisfy (h) above. Neither issuers nor intermediaries are permitted to offer investment advice. In addition, the bill would amend Section 12(g)(5) of the Securities Exchange Act of 1934 (the Exchange Act) to exclude from the calculation of the number of stockholders of record of a company for purposes of required company registration under the Exchange Act, persons who purchase securities under the new Section 4(6) exemption.

H.R. 2940 would amend Section 4(2) of the Act and require the SEC to amend Rule 506 of Regulation D under the Act to provide that the prohibition against general solicitation or general advertising shall not apply to sales made pursuant to Rule 506, provided that all purchasers of the securities are “accredited investors”, as defined in Rule 501(a) under the Act.

Click here to read H.R. 2930.
Click here to read H.R. 2940.

SEC Approves New Exchange Rules to Toughen Listing Standards for Reverse Merger Companies

On November 9, the Securities and Exchange Commission approved new rules proposed by the New York Stock Exchange LLC, NYSE Amex LLC and the NASDAQ Stock Market LLC that toughen the listing standards for issuers that become public through reverse mergers. A reverse merger is a transaction in which an unlisted private operating company becomes public via a merger with a publicly traded shell company, which is generally a company with no material business operations.

As described in the April 29 and August 19 editions of the *Corporate and Financial Weekly Digest*, the rules were proposed in response to widespread concerns about accounting fraud by certain companies with foreign operations. Generally, the new rules require that a reverse merger company trade for at least one year on the over-the-counter market or on another regulated U.S. or foreign exchange following the SEC filing reporting its business combination and timely file all periodic reports with the SEC, including at least one annual report, prior to being listed on any of the three exchanges. Additionally, the rules require a minimum $4 a share price for a sustained period and for at least 30 of the 60 trading days immediately prior to its listing application and the exchange's approval to list.

Each of the three exchanges provided an exemption from the new rules for a reverse merger company if (i) it is listing on an exchange in connection with a firm-commitment underwritten public offering that generates proceeds to the company of at least $40 million or (ii) following its business combination filing with the SEC, it has met the one-year trading requirement and filed at least four annual reports with the SEC containing audited financial statements.

For more information, click here.

LITIGATION

Court Addresses Appropriate Procedure for Lead Plaintiff Appointment

The United States District Court for the Eastern District of New York recently addressed the question of how to designate a lead plaintiff in a class action brought under the Private Securities Litigation Reform Act (PSLRA) where the original named plaintiff withdraws.

Plaintiff Steven Endress filed a securities fraud class action on behalf of all persons who purchased the publicly traded common stock of Gentiva Health Services (Gentiva) during the relevant class period. A pension fund that purchased Gentiva stock during the class period filed a motion to intervene as a plaintiff in that action. After Endress filed a motion to withdraw, four other plaintiffs subsequently filed essentially identical class action claims against Gentiva. All five plaintiffs sought to be named lead plaintiff for the class in the proposed consolidated action.

The court found that none of the proposed lead plaintiffs had complied with the PSLRA requirement that the lead plaintiff must either file the original complaint or move for appointment within 60 days of the plaintiff's publication of notice that a case has been filed. Instead, the original named plaintiff's motion to withdraw touched off a "race to the courthouse" in which proposed lead plaintiffs filed essentially identical actions and sought to be named lead plaintiff.

Finding that judges "are not referees at prize fights but functionaries of justice," the court held that in light of the intent and purposes of the PSLRA, it would determine whether any additional class members desired to serve as named plaintiff prior to the court appointing a lead plaintiff. The court therefore deemed a movant as eligible to be appointed lead plaintiff if there was a motion for appointment filed within 60 days of the original lead plaintiff's withdrawal, and held that any member of the putative class could also file a motion to be appointed lead plaintiff.

Endress v. Gentiva Health Services, Inc., No. 10-CV-5064 (ADS)(WDW) (E.D.N.Y. Nov. 2, 2011)

EXECUTIVE COMPENSATION AND ERISA

DOL Finalizes Investment Advice Guidance for 401(k) Type Plans

The Department of Labor (the DOL) recently issued guidance that clarifies how advisers can provide investment advice to retirement plan participants in a manner that protects both the participant and the provider. The final rule, released by the DOL on October 24, allows investment advisers to provide individualized investment advice to participants in account balance plans, (401(k) plans, profit-sharing plans, and IRAs) if either (i) the advice is provided pursuant to a computer model certified as unbiased and as applying generally accepted investment theories, or (ii) the adviser is compensated on a "level-fee" basis (i.e., fees do not vary based on investments selected by participants).

In adopting the final rule, the DOL was balancing several considerations. For example, the DOL did not want to adopt a rule which might allow advice to be provided by an adviser who could have a conflict of interest. On the other hand, because retirement plan savings are expected to account for such a large portion of Americans' retirement income, the DOL wanted to ensure that participants have access to quality investment advice so that, among other things, they might be more likely to pay lower fees, engage in less excessive or poorly timed trading, and more adequately diversify their portfolios.

In order to ensure the protection of both the investment advisers and plan participants, reliance on the final rule requires compliance with many conditions. Some of those conditions include:

- requiring that a plan fiduciary (independent of the investment adviser) authorize the advice arrangement;
- satisfying certain recordkeeping requirements;
- mandating that the computer model, if used, must be certified in advance by an independent expert (as well as qualifications and selection procedures for identifying the independent certifying expert);
- ensuring that a "level-fee" investment advice provider does not receive compensation from any party on the basis of investment alternatives selected by participants; and
- completing an independent annual audit of the investment advice arrangement to ensure compliance with the final rule.

The DOL estimates that approximately 134,000 plans covering 17 million participants will offer investment advice to participants pursuant to the final rule, and that approximately 3.5 million participants will actually seek investment advice thereunder. Based on those numbers, the DOL expects the net financial benefit of the final rule to be between $5 billion and $13 billion.

The final rule will become effective on December 27, and will be applicable to transactions occurring on or after that date.

The final rule can be found here.

BANKING

Change in Virtual Data Room Used by the FDIC When Marketing Failing Financial Institutions

On November 7, the Federal Deposit Insurance Corporation (FDIC) announced that it is changing the virtual data room hosting company used to help market failing financial institutions. Beginning in November 2011, the FDIC will begin using the RR Donnelley (the site is known as "Venue") instead of IntraLinks, which will continue to host projects initiated before November 2011 until they are resolved.

For more information, click here.

Consumer Financial Protection Bureau To Identify and Eliminate Unnecessary and Burdensome Regulations

Raj Date, the acting head of the Consumer Financial Protection Bureau, announced on November 9 that the bureau will begin a targeted review to identify and address outdated, unnecessary and unduly burdensome

regulations. Speaking before the American Bankers Association's Community Bankers Council, Mr. Date stated, "I have been a vocal critic of the efficiency and effectiveness of bank regulation for my entire career. As an institution, we have no emotional attachment to the way things have been done in the past. If it doesn't make sense, we're going to stop doing it." Date noted that the bureau has inherited from other agencies numerous regulations that have been on the books for years, and invited bankers to provide input to identify the rules that should be priority candidates for review.

To visit the Consumer Financial Protection Bureau's website, click here.
For more information about the review, click here.

FinCEN Issues FAQs Related to Prepaid Access Rule

On November 2, Treasury's Financial Crimes Enforcement Network (FinCEN) issued a list of Frequently Asked Questions (FAQs) related to its prepaid access rule originally issued by FinCEN in July. The FAQs were issued to help providers and sellers of prepaid access in understanding the scope of the recordkeeping and reporting requirements related to the prepaid card business under the Bank Secrecy Act (BSA).

The FAQs discuss various FinCEN positions related to prepaid access including what happens when none of the participants in a prepaid program register with FinCEN as the "provider of prepaid access" (in which case the provider of such access will be the "participant in the program with principal oversight and control over the prepaid program"). In addition, the FAQs discuss how it will analyze whether a business is a "seller" of prepaid products if it provides non-depository reloads to prepaid access. Finally, the FAQs make clear that a prepaid card program manager that is not the provider of prepaid access has no obligations under the prepaid access rule.

For more information, click here.

UK DEVELOPMENTS

FSA Fines Private Investor $9.6 million for Market Abuse

On November 9, the UK Financial Services Authority (FSA) announced that it had fined Rameshkumar Goenka (Goenka), a Dubai based private investor, $9,621,240 for manipulating the closing price of Reliance Industries (Reliance) securities on the London Stock Exchange (LSE).

The $9,621,240 fine is the largest ever imposed by the FSA on an individual for market abuse. It comprises a penalty of $6,517,600 and a restitution element of $3,103,640. The FSA has stated that the restitution element will be used to reimburse the counterparty which overpaid Goenka that sum as a result of his market abuse.

Goenka held an over-the-counter (OTC) structured product based on Reliance global depositary receipts (GDRs) which matured on October 18, 2010. The pay-out depended on the LSE closing price of Reliance shares on that day. On October 18, 2010 Goenka placed a series of trades in the final seconds of the LSE's closing auction with the intention of increasing the closing price of the Reliance securities above a certain level and ensuring that other market participants did not have sufficient time to respond before the closing price was determined. As a result of Goenka's market manipulation, which increased the Reliance closing price, Goenka's counterparty overpaid him $3,103,640.

The FSA stated that the amount of the fine took into account the seriousness of the market abuse and also the fact that Goenka intended to engage in similar conduct on another occasion in relation to another structured product and was prevented from doing so only by factors outside his control.

Genka received a early settlement discount of 30% on the penalty element for settling at an early stage of the FSA's investigation. If Goenka had not settled early the financial penalty element of the fine would have been $9,310,920 – three times the profit made as a result of the market abuse conduct. The total fine (including the restitution element) would in that event have been $12,414,560.

For more information, click here.

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