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Corporate and Financial Weekly Digest

November 16, 2007

A Note from the Editor

Please note that *Corporate and Financial Weekly Digest* will not be published next Friday, November 23 due to the Thanksgiving Holiday. The next issue will be distributed on November 30.

Robert Kohl

SEC/Corporate

SEC Adopts Three New Small Business Initiatives

On November 15, the Securities and Exchange Commission adopted three rules aimed at modernizing disclosure requirements and capital raising activities of smaller public companies.

The three sets of rules are:

Smaller Reporting Company Regulatory Relief and Simplification

The final rules, among other things:

- replace the current "small business issuer" category with a new expanded category of "smaller reporting companies" having less than $75 million in public equity float;
- expand eligibility for the SEC's scaled disclosure and reporting requirements for smaller companies by allowing the newly defined category of smaller reporting companies to use the scaled disclosure requirements;
- move 12 non-financial scaled disclosure item requirements from Regulation S-B into Regulation S-K (the scaled disclosure requirements will only be available to smaller reporting companies);
- amend financial statement requirements in Item 310 of Regulation S-B into new Article 8 of Regulation S-X, and amend these requirements to provide a scaled disclosure option for smaller reporting companies, requiring two years of balance sheet data instead of one year; and

SEC/CORPORATE

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- permit smaller reporting companies to elect to comply with scaled financial disclosure and non-financial disclosure on an item-by-item basis.

The effective date for these rules will be 30 days after their publication in the *Federal Register*.

Revisions to Rule 144 and Rule 145 of the Securities Act

The amendments to Rule 144 of the Securities Act include:

- shortening the holding period for restricted securities of reporting companies to six months;
- substantially simplifying compliance with Rule 144 of the Securities Act for non-affiliates by allowing non-affiliates of reporting companies to freely resell restricted securities after satisfying a six-month holding period (subject only to the public information requirement of Rule 144(c) of the Securities Act until the securities have been held for one year); and
- for affiliates' sales, revising the manner of sale requirements for equity securities and eliminating them for debt securities and relaxing the volume limitations for debt securities.

The amendments to Rule 145 of the Securities Act:

- eliminate the presumptive underwriter provision except with respect to transactions involving blank check or shell companies; and
- revise the resale provisions of Rule 145(d) of the Securities Act.

These amendments will be effective 60 days after their publication in the *Federal Register*.

Exemption of Compensatory Employee Stock Options from Registration under Section 12(g) of the Exchange Act

The two amendments to Exchange Act Rule 12h-1:

- provide an exemption for private non-reporting issuers from Exchange Act Section 12(g) registration for compensatory employee stock options issued under employee stock option plans; and
- provide an exemption for issuers that are required to file reports under the Exchange Act pursuant to Exchange Act Section 13 or Section 15(d) from Exchange Act Section 12(g) registration for compensatory employee stock options.

The exemptions will apply only to an issuer's compensatory employee stock options and will not extend to the class of securities underlying those options.

These amendments will be effective as soon as they are published in the *Federal Register*.

The full text of the detailed releases concerning these items will be posted to

the SEC website as soon as possible.

http://www.sec.gov/news/press/2007/2007-233.htm

SEC Adopts Rules Allowing Foreign Issuers to Report without IFRS-GAAP Reconciliation

On November 15, the Securities and Exchange Commission announced the approval of rule amendments permitting foreign private issuers to include in their U.S. filings financial statements prepared using International Financial Reporting Standards as issued by the International Accounting Standards Board without reconciliation to U.S. Generally Accepted Accounting Principles.

Chairman Cox also announced that the SEC will convene two roundtables in December to collect more feedback from the public on the issue of giving U.S. domestic issuers the same option that foreign issuers have in our markets to use either IFRS or GAAP.

The rule amendments will take effect 60 days after they are published in the Federal Register and apply to financial statements covering years ended after Nov. 15, 2007. The full text of the detailed release concerning the rule amendments will be posted to the SEC website as soon as possible.

http://www.sec.gov/news/press/2007/2007-235.htm.

Broker Dealer

SEC Approves New "Complex Trade" Definition Proposed by Major Option Exchange

The Securities and Exchange Commission has approved changes to the rules governing the operation of the Intermarket Option Linkage to amend the definition of "complex trade" to include stock-option trades. The new definition, proposed and to be adopted concurrently by the American Stock Exchange, Boston Stock Exchange, Chicago Board Options Exchange, International Securities Exchange, and NYSE ARCA, will include the execution of a stock-option order to buy or sell a stated number of units of an underlying stock or convertible security coupled with the purchase of option contracts on the opposite side of the market representing either (a) the same number of units of the underlying stock or convertible security, or (b) the number of units of the underlying stock or convertible security necessary to create a delta neutral position. In no case can the ratio of option contracts per unit of trading of the underlying stock or convertible security established for that series by the Options Clearing Corporation exceed 8:1.

http://a257.g.akamaitech.net/7/257/2422/01jan20071800/edocket.access.gpo.gov/2007/pdf/E7-22165.pdf

National Association of Realtors Requests Broker-Dealer Exemption

The National Association of Realtors (NAR) has petitioned the Securities and Exchange Commission for exemption under Sections 15(a)(2) and 36(a) of the Securities Exchange Act of 1934 from the broker-dealer registration requirements for real estate brokerage firms and licensed real estate agents who sell individual tenant-in-common interests in real property (TIC Security) and receive a real estate advisory fee either from the purchaser or issuer of the TIC Security. TIC Securities are sold by a sponsor through a broker-dealer acting as placement agent. The SEC estimates there are 5,304 TIC Security Transactions a year that would include 800 commercial real estate professionals and approximately 150 selling broker-dealers.

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Conditions undertaken by NAR included: (a) a real estate advisory fee could only be paid to an experienced, knowledgeable and licensed commercial real estate professional predominantly engaged in the sale of real estate other than TIC Securities; (b) each client would receive at closing a deed to his undivided factional interest in the TIC Security; (c) the client would enter into a written agreement with the real estate participant; (d) the agreement would disclose the maximum real estate advisory fee or a formula for its computation; (e) the client is advised as to the characteristics of TIC Securities and may inspect the subject property; (f) the real estate participant cannot (1) advertise TIC Securities, (2) share the fee with anyone not listed in the agreement with the client; (3) handle customer funds or securities in a TIC transaction, (4) negotiate a TIC purchase on behalf of the client, (5) act as a "purchaser's representative" under Regulation D, (6) participate in structuring an offering of TIC Securities, or (7) assist a client to obtain funds to buy a TIC Security other than to provide a list of potential lenders; (g) the commercial real estate representative can not be subject to a statutory disqualification under the Exchange Act and must certify such at the closing to the selling broker-dealer; (h) the selling broker-dealer must perform a suitability analysis of the customer and if it determines the TIC Security is unsuitable for the customer, not effect the transaction without the customer's written affirmation that it wishes to proceed. The SEC estimates that will be the case in 5% of the transactions.

The petition is open for public comment.

http://www.sec.gov/rules/other/2007/34-56779.pdf

Investment Companies and Investment Advisers

SEC's IM Director Donohue Asks Fund Directors How SEC Can Help – Valuation Issues Raised

In a speech on November 6 before the Investment Company Directors Conference in Washington, Andrew "Buddy" Donohue, Director of the Securities and Exchange Commission Division of Investment Management, described the SEC's mutual fund Director Outreach Initiative (DOI). The DOI's purpose is to answer the question: "What can or should the Commission do in order to aid fund directors in the performance of their duties?" Donohue was perplexed by the general lack of response from fund directors when he asked them, "where do you add value for shareholders and the fund?" Given the recent events in the sub-prime market, the "key area where fund directors add value for shareholders is in the fair valuation of portfolio securities," stated Donohue. "If you are having difficulty pricing a security or if securities pose a liquidity challenge, query whether those securities belong in a mutual fund." Based on DOI feedback, Donohue also highlighted (i) the nature of the comments the SEC received concerning Rule 12b-1 fees, (ii) the obligation of directors to monitor soft dollar payments, including a current effort by Donohue's staff to issue guidance on a director's oversight responsibilities for fund trading practices and (iii) the propriety of delegating board responsibilities to the fund's chief compliance officer.

http://www.sec.gov/news/speech/2007/spch110607ajd.htm.

SEC's OCIE Associate Director Gohlke Outlines Extensive Line of Director Inquiry About Fund's Use of Derivatives

At a November 8 program on "Funds' Use of Derivatives" sponsored by the Mutual Fund Directors Forum in New York, Gene Gohlke, Associate Director of the Securities and Exchange Commission Office of Compliance Inspections and Examinations, offered an extensive outline of questions that mutual fund directors should pursue if their funds are investing in derivatives. After noting

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the oversight responsibilities of directors, Gohlke presented detailed questions focusing on 12 areas of risk attendant to derivatives investing. These focus areas cover the adviser's intellectual and financial resources, due diligence processes, risk management functions, risk disclosure, prevention of inappropriate use of non-public fund derivatives information, illiquidity measuring and monitoring, embedded or economic leverage measuring and monitoring, valuation, sufficiency of back office services, effectiveness of compliance procedures and compliance testing, the chief compliance officer's role, and types of derivative risk/return information provided to the fund's board regularly and under exceptional circumstances.

http://www.sec.gov/news/speech/2007/spch110807gg.htm

Banking

OTS Issues Advance Notice of Proposed Rulemaking Regarding TFRs

On November 13, the Office of Thrift Supervision (OTS) issued an advance notice of proposed rulemaking (ANPRM) seeking comments with respect to the possible revision of the type of financial data collection reports thrift institutions file with the OTS.

More specifically, the OTS seeks comment "identifying information that the thrift industry and the public would need to analyze a proposal to convert from the Thrift Financial Report (TFR) to the Consolidated Reports of Condition and Income (CALL Report) used by other federal banking regulators and to amend any OTS rules that would be affected by such a change." The ANPRM states that, should the CALL Report be used by thrift institutions, such institutions would still be required to file certain information currently collected on the TFR that is not included on the CALL Report.

At the close of the comment period, the OTS stated that it will review the submissions it has received and conduct any further necessary research. The agency will then publish a second notice and solicit comments on whether to convert from the TFR to the CALL Report.

According to the OTS's accompanying press release, the ANPRM was issued in response to thrift industry participants who requested the change. (72 *Federal Register* 64003, 11/14/07).

Comments are due by January 14, 2008.

BANKING

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United Kingdom Developments

UK Covered Bonds Regime to be Introduced from March 2008

The UK Government announced on November 8, that it will introduce a new covered bonds regime with effect from March 6, 2008. Originally, the Government had intended to implement the regime from January 2008, as described in the July 27, 2007 edition of *Corporate and Financial Weekly Digest*. There is currently no UK legislative framework under which UK issuers can issue covered bonds which are permitted investments under Article 22(4) of the EU Undertakings for Collective Investment in Transferable Securities (UCITS) Directive for funds established under the UCITS Directive.

The UK Treasury and the Financial Services Authority have been considering proposals for a covered bonds regime that complies with the UCITS Directive requirements. It is anticipated that a UCITS compliant regime will enable UK issuers to access a larger investor base.

The proposals were first announced in July 2007 and the consultation closed

UK DEVELOPMENTS

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last month. A summary of all responses together with proposed regulations is expected to be published in January 2008.

www.hm-treasury.gov.uk/newsroom_and_speeches/press/2007/press_120_07.cfm

FSA Proposes Disclosure for UK Contracts for Difference

On November 12, the Financial Services Authority (FSA) published a consultation paper proposing greater disclosure of significant "economic interests" in shares held through derivatives such as Contracts for Difference (CFDs). The FSA's position has gradually evolved since in CP06/4, as described in the April 9, 2006 edition of *Corporate and Financial Weekly Digest*, it announced that it was not minded to expand the shareholding disclosure regime to apply to derivatives. It has now concluded that potential market failures could occur where CFDs are used on an undisclosed basis to influence corporate governance and build up stakes in companies. The Financial Services Authority has stated that such failures, although not widespread, need to be addressed to ensure that market confidence and efficiency are maintained.

CFDs currently fall outside the scope of the FSA's disclosure and transparency rules although disclosure of dealings in CFDs is required under Takeover Panel rules during an offer period.

The consultation proposes two alternative approaches: (i) strengthening the current regime by requiring disclosure in defined circumstances of CFDs that reference 3% or more of the total voting rights attached to a company's shares, or (ii) introducing a general disclosure regime which would require CFD holders to reveal all economic interests of 5% or more in a company's shares.

The consultation period ends on February 12, 2008.

www.fsa.gov.uk/pages/Library/Policy/CP/2007/07_20.shtml

Study Identifies Keys to AIM's Success

On November 13, the London School of Economics published a research report, *From Local to Global – The rise of AIM as a stock market for growing companies*, commissioned by the London Stock Exchange. The report reviews the growth and development of AIM since its inception in 1995 and highlights that the amount of capital raised on AIM has increased from £2 billion ($4.1 billion) in 2003 to £15.7 billion ($32.15 billion) in 2006.

According to the report, since 1995 some 2,300 British and 400 foreign companies have come to AIM, raising a total of £49 billion ($100 billion), of which over 40% has been in the form of further issues.

The report attributes AIM's success to several key factors including: (i) distinctive regulation, (ii) broad market profile, (iii) strong after-market performance and low failure rates, and (iv) strong liquidity for larger securities.

www.londonstockexchange.com/en-gb/about/Newsroom/pressreleases/2007/AIM+Study+Identifies+Keys+To+Success.htm

FSA Update on Funds of Alternative Investment Funds

On November 14, the Financial Services Authority (FSA) issued an update on its proposals to allow UK retail consumers to invest in funds of hedge funds and other alternative investments sold by UK authorized firms.

The FSA had planned to issue a policy statement and final rules at the end of this year which would have allowed the development of a Funds of Alternative Investment Funds (FAIFs) vehicle for the retail market, as described in the March 30, 2007 edition of *Corporate and Financial Weekly Digest.*

There remain a number of tax issues that are currently being considered in conjunction with proposed changes to the UK's offshore funds regime, as described in the October 19, 2007 edition of *Corporate and Financial Weekly Digest,* and the FSA now consider it appropriate to delay publication of its FAIF proposals until early 2008.

www.fsa.gov.uk/pages/Library/Communication/PR/2007/116.shtml

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Court Compels Broker-Dealer to Arbitrate Investors' Claims

Finding that investors were "customers" of a retail broker-dealer for purposes of the NASD's Code of Arbitration, a federal district court compelled the broker-dealer to arbitrate the investors' securities fraud claims. The broker-dealer argued that because the investors' claims were premised upon purportedly false statements made by an employee/registered representative prior to his employment with the broker-dealer, NASD Rule 10301 – which requires any dispute between a customer and an NASD member to be arbitrated under the NASD Code – was inapplicable.

Rejecting this argument, the Court explained that in the Eighth Circuit, a customer for purposes of Rule 10301 is anyone engaged in an investment relationship with a NASD member. The Court found that regardless of when the registered representative made the alleged misrepresentations, there was no dispute that the investors purchased additional shares in the company that was the subject of the alleged misrepresentations when the registered representative was employed by the broker-dealer. Accordingly, the Court ruled that the investors were customers of the broker-dealer and that the broker-dealer was therefore required to arbitrate their claims before the NASD. (*O.N. Equity Sales Company v. Prins*, 2007 WL 3286406 (D. Minn. Nov. 7, 2007))

District Court Dismisses Securities Fraud Claim Against Company's Auditor

Granting defendant auditor's motion to dismiss plaintiffs' class action securities fraud claims, a federal district court held, among other things, that defendant could not be found liable under section 10(b) of the Securities Exchange Act of 1934 or Rule 10b-5 for statements that the auditor's client – but not the auditor – made to the public. Plaintiffs argued that the defendant auditor certified as true a public company's materially false quarterly financial statements and, thereby, shared liability with the company for the misstatements. Rejecting this argument, the Court emphasized that pursuant to the Exchange Act, there is no liability for merely aiding and abetting a false statement to the investing public because, under United States Supreme Court precedent, section 10(b) "prohibits only the *making* of a material misstatement (or omission)."

Although plaintiffs alleged that the auditor "signed off" on the purportedly misleading quarterly financial statements with knowledge that investors would rely on them once its client released them, plaintiffs did not allege that the auditors themselves made, or caused to be made, any misrepresentation in connection with the quarterly statements. After characterizing this component of the plaintiffs' claim as "a textbook case of aiding and abetting," the Court ruled that the allegations were insufficient. (*In re aaiPharma, Inc. Securities Litigation*, 2007 WL 3342286 (E.D.N.C. Nov. 6, 2007))

CFTC

CFTC Extends Registration Exemption to Certain Foreign Persons

The Commodity Futures Trading Commission has adopted amendments to Part 3 of its regulations to codify its policies with respect to the registration obligations of foreign persons who solicit and accept orders for execution on U.S. markets on behalf of non-U.S. customers. As amended, Regulation 3.10 exempts from registration certain foreign firms that have only foreign customers and clear designated contract market business for such customers on an omnibus basis through a registered futures commission merchant, as well as foreign persons acting as introducing brokers, commodity trading advisors or commodity pool operators solely on behalf of foreign persons. The CFTC also amended Regulation 3.12 to exempt from registration as an associated person (AP) any individual located in the foreign branch office of a CFTC registrant that acts as an AP solely on behalf of non-U.S. customers.

http://www.cftc.gov/stellent/groups/public/@lrfederalregister/documents/file/e7-22110a.pdf

CFTC Allows U.S. Sale of Security Index Futures by Swedish Exchange

On November 13, the Commodity Futures Trading Commission issued a no-action letter to OMX Nordic Exchange Stockholm AB (OMX Stockholm) authorizing the offer and sale in the U.S. of OMX Stockholm's futures contract based on the VINX30 Index. The CFTC explicitly conditioned the relief on OMX Stockholm's continued compliance with all regulatory requirements imposed by the Swedish Financial Supervisory Authority and the applicable laws and regulations of Sweden.

http://www.cftc.gov/stellent/groups/public/@lrletter07/documents/letter/07-21.pdf

CFTC

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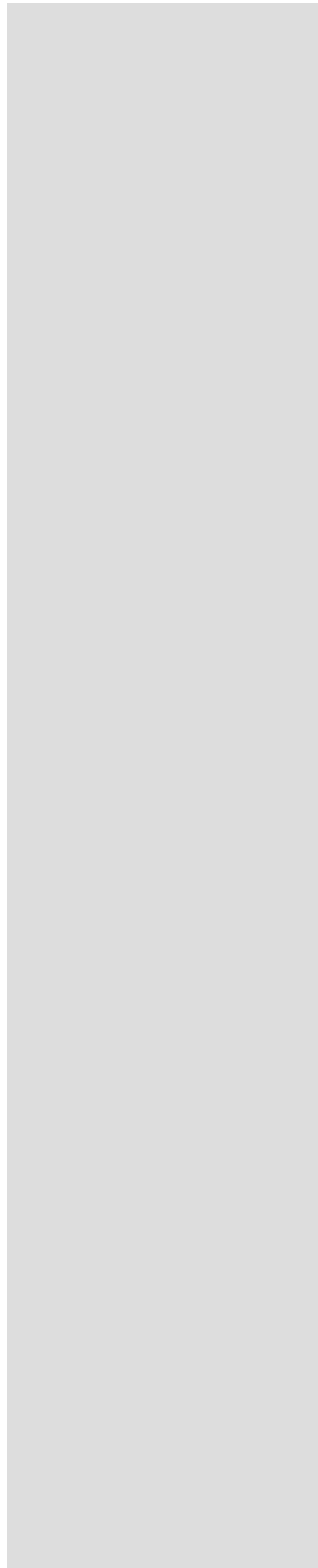

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