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CORPORATE & FINANCIAL
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SEC/CORPORATE

Division of Corporation Finance Updates Financial Reporting Manual

On October 4, the Division of Corporation Finance of the Securities and Exchange Commission released an updated Financial Reporting Manual containing revisions to certain sections as of June 30, 2012. The updated Financial Reporting Manual has not yet been revised to reflect the financial reporting and other requirements under the Jumpstart Our Business Startups Act (JOBS Act) for emerging growth companies (EGCs). Therefore, the Financial Reporting Manual should be read in conjunction with the JOBS Act and staff guidance related to financial reporting and other requirements for EGCs.

The other revisions to the Financial Reporting Manual clarify the following:

- proxy statement financial statement requirements for the disposal of a business;
- auditor association with amounts from inception in development stage companies;
- application of Public Company Accounting Oversight Board auditor requirements for financial statements filed pursuant to a reverse merger; and
- Form 8-K reporting and financial statement requirements in a reverse acquisition with a domestic registrant that is not a shell company.

Current revisions are marked with the date tag “Last updated: 6/30/2012” to identify the changes.

To view the updated Financial Reporting Manual, click here.

BROKER DEALER

SEC National Exam Program Initiative to Conduct Exams of Newly Registered Investment Advisers

The Securities and Exchange Commission has sent a letter dated October 9, 2012 (Letter), to investment advisers that registered with the SEC on or after the July 21, 2011 effective date in which the rules under the Dodd-Frank Wall Street Reform and Consumer Protection Act became effective (Newly Registered Advisers). The Letter introduces Newly Registered Advisers to the SEC’s National Exam Program (NEP) administered by the Office of Compliance Inspections and Examinations (OCIE) and provides information about upcoming examinations of certain Newly Registered Advisers and the topical areas that may be examined.

In the Letter, the SEC states that the NEP is launching an initiative to conduct focused, risk-based examinations of Newly Registered Advisers that will take place over the next two years (Presence Exam Initiative) in three phases—the engagement phase, the examination phase and the reporting phase.

The Letter alerts recipients to the fact that during the current engagement phase of the Presence Exam Initiative, the NEP staff is reaching out to Newly Registered Advisers and informing them of their obligations under the Investment Advisers Act of 1940 and the rules thereunder, the Presence Exam Initiative and OCIE's practice of engaging directly with firms' senior management. The Letter provides resource references for Newly Registered Advisers to review.

The Letter informs Newly Registered Advisers that during the examination phase of the Presence Exam Initiative the NEP staff will review higher-risk areas of the business and operations of selected Newly Registered Advisers, including marketing, portfolio management, conflicts of interest, safety of client assets (i.e., custody) and valuation procedures. After the examination phase, the NEP intends to report its observations to the SEC and the public.

Click here to read the SEC's October 9, 2012 letter to Newly Registered Investment Advisers.

CFTC

NFA Adopts Requirements for FCMs, IBs, CPOs and CTAs Dealing in Swaps

On October 3, the National Futures Association (NFA) announced that recent amendments to NFA Bylaw 301, relating to approval requirements for "swaps firms" and "swaps APs," will take effect on January 1, 2013. Under the amended bylaw, any NFA member that is registered with the Commodity Futures Trading Commission as a futures commission merchant (FCM), introducing broker (IB), commodity pool operator (CPO) or commodity trading advisor (CTA) and that engages in swap activities that are subject to the jurisdiction of the CFTC must be identified as a "swaps firm" on the firm's Form 7-R on the NFA's Online Registration System. In addition, any associated person (AP) of a swaps firm that engages in swap activities on behalf of the firm in one of the above capacities must be identified as a swaps AP on the Form 8-R for that AP. An existing registrant wishing to be a "swaps firm" must amend its Form 7-R and the Form 8-R only for each AP that will be a swaps AP. A new registrant must respond to the relevant questions for each of its APs. An AP designated as a swaps AP has no additional proficiency examination requirement. (NFA has also provided relief from the examination requirement for certain other APs as summarized below in "NFA Provides Relief from Proficiency Exam Requirements for Certain CPOs, CTAs and Other Swaps Firms".) An NFA member that is designated as a swaps firm must have at least one principal registered as a swaps AP at all times. Although the amendments do not take effect until January 1, 2013, members and APs may request swap designation effective immediately.

NFA's Notice to Members I-12-24, which provides additional information about the amendments, is available here.

NFA Provides Relief from Proficiency Exam Requirements for Certain CPOs, CTAs and Other Swaps Firms

Effective October 3, the National Futures Association (NFA) has amended its registration rules 401 and 402 to exempt associated persons (APs) of NFA member futures commission merchants, introducing brokers, commodity pool operators (CPOs) and commodity trading advisors from the NFA proficiency (Series 3 examination) requirements if the AP's activities that are subject to CFTC jurisdiction are limited to swaps, plus in the case of APs of CPOs, a de minimis amount of other commodity interest activity. APs who indicate on Form 8-R that their activities will be limited solely to swaps will be automatically exempt. A CPO who would be able to claim exemption or exclusion from CPO registration available to firms engaging in de minimis trading under either CFTC Rule 4.13(a)(3) or CFTC Rule 4.5(c)(2)(iii)(A) or (B) if swaps were not included in the calculation of the commodity interest trading of the pool must request waiver of the Series 3 requirement for the APs it sponsors in writing. Any NFA member that obtains a waiver for its APs must notify NFA if the AP or the sponsor becomes ineligible for the waiver.

NFA's Notice to Members I-12-24, which provides additional information about these exemptions and detailed instructions for making any necessary filings, is available here.

CFTC Issues Guidance on Swap Data Reporting

In separate responses to frequently asked questions issued on October 10 and 11 (each, an FAQ), the Commodity Futures Trading Commission (CFTC) has provided additional clarification regarding swap data reporting obligations.

On October 10, the CFTC issued an FAQ related to the start of swap data reporting. The FAQ addresses a variety of issues and concerns that have been raised by market participants, including: the date by which Swap Dealers (SDs) must begin to report swap data to a Swap Data Repository (SDR), the date by which Major Swap Participants (MSPs) must begin to report swap data to an SDR, the date by which a non-SD/MSP reporting counterparty must begin to report swap data to an SDR, the date by which "historical swaps" must begin to be reported, and the date by which Legal Entity Identifiers must be obtained to comply with Part 45 and Part 46 of the CFTC regulations.

On October 11, the CFTC issued a second FAQ related to the reporting of cleared swaps. The FAQ addresses a variety of issues and concerns that have been raised by market participants regarding the mechanics of reporting, including how cleared swap transactions will be reported to SDRs, the respective reporting obligations of SDs, MSPs, and other swap counterparties, and the ability of swap counterparties to select the SDR to which swap data will be reported and designate which party is to report any creation and continuation data.

The FAQ further addresses several reporting obligations for derivatives clearing organizations (DCOs), swap execution facilities (SEFs), and designated contract markets (DCMs). Among other things, the FAQ clarifies that a DCO, SEF or DCM that is also registered as, or affiliated with, an SDR is not permitted to require counterparties to use that "captive" SDR to report swap transactions.

The October 10 FAQ is available here.

The October 11 FAQ is available here.

LITIGATION

Court Grants Preliminary Injunction in Case Involving General Partnership Interests

A California district court granted the Securities and Exchange Commission's motion for a preliminary injunction against defendants who were selling general partnership interests in parcels of land. The court determined that the SEC had made a *prima facie* showing that the general partnership interests at issue could be designated "securities," thus triggering the SEC's enforcement authority. In making such determination, the court employed a test, known as the *Williamson* test, devised by the Fifth Circuit and adopted by the Ninth Circuit (the federal appellate court for California). The general partnerships in this case owned a fraction of a parcel of land and therefore only had partial control over the land. The court found that the SEC had made a *prima facie* case under *Williamson* by demonstrating that the defendants' likely involvement in selling the parcel of land in which the general partnerships were invested, their pivotal operational role with respect to the general partnerships, the fractional nature of the general partnerships' interest in the land and the apparent use of investors' IRA funds cumulatively satisfied the court that the SEC had made a *prima facie* case that the general partnership interests at stake were securities.

SEC v. Schooler, No. 12-cv-2164, 2012 WL 4761917 (S.D.Cal. Oct. 5, 2012).

Court Finds Plaintiff's New Evidence Insufficient to Satisfy PSLRA Pleading Requirements

In a securities fraud action, a Colorado district court denied a plaintiff employees' retirement plan's motion for relief from a final judgment that dismissed the plaintiff's original complaint because it did not satisfy the pleading requirements of the Private Securities Litigation Reform Act (PSLRA). The plaintiff filed the motion after obtaining transcripts of testimony given to the Securities and Exchange Commission by the defendants, the CEO and COO of C-BASS, a firm in the business of buying, packaging and reselling subprime mortgage loans. Pointing to SEC transcripts, the plaintiff contended that the CEO and COO had made fraudulent statements regarding C-BASS during a quarterly conference call regarding another company. The court analyzed the statements at issue and found that the transcripts did not show that the statements were false. In one instance, the court found that although the defendants knew July 2007 would be a volatile month, nothing in the transcripts showed that, as the plaintiff maintained throughout the case, the defendants knew as of July 19, 2007, that C-BASS was about to be overwhelmed by margin calls from lenders. Having found that the plaintiff's new evidence was not likely to change the outcome of the case as required by Federal Rule of Civil Procedure 60(b)(2), the court denied plaintiff's motion for relief from judgment.

Fulton County Employees' Retirement System v. MGIC Inv. Corp., No. 8-C-0458, 2012 WL 4739797 (E.D.Wis. Oct. 3, 2012).

BANKING

FDIC, OCC and the Federal Reserve Approve Final Rules Regarding Large Bank Stress Tests and FDIC Issues Separate Rule on Large Bank Assessment Pricing

On October 9, the Federal Deposit Insurance Corporation (FDIC), along with the Office of the Comptroller of the Currency (OCC) and the Board of Governors of the Federal Reserve System (Federal Reserve) (collectively, the Agencies), announced publication of their final rules regarding company-run stress testing required by the Dodd-Frank Wall Street Reform and Consumer Protection Act. The rules apply to covered institutions with total consolidated assets greater than $10 billion.

The final rules implement Section 165(i)(2)(A) of the Dodd-Frank Act, which requires all financial companies with total consolidated assets of more than $10 billion that are regulated by a primary federal financial regulatory agency to conduct an annual company-run stress test. The final rules also require institutions with assets greater than $50 billion to begin conducting annual stress tests this year, although the Agencies each preserved their authority to allow covered institutions above $50 billion to delay implementation on a case-by-case basis where warranted. It is expected that some holding companies that own multiple banks, and other non-banking companies that have never performed stress tests, may request extensions.

The rules, as was widely expected due to industry complaints, delay implementation for covered institutions with total consolidated assets between $10 billion and $50 billion until October 2013, one year later than originally planned. For institutions with assets greater than $50 billion that are required to begin stress testing this year, the Agencies anticipate releasing stress-testing scenarios to those institutions in November. These three scenarios will be "stable," "adverse" and "severely adverse." Those institutions will use their data as of September 30, 2012, to conduct the stress test. Results are due in January 2013, and a covered institution must make public the results of the stress test under severely adverse conditions in March 2013.

For institutions that have assets between $10 billion and 50 billion, public disclosure will not be required until 2015.

To view the summary by the FDIC, click here.

To view the summary by the OCC, click here.

To view the summary by the Board of Governors of the Federal Reserve System for banking organizations other than covered companies, click here.

To view the summary by the Board of Governors of the Federal Reserve System for covered companies, click here.

UK DEVELOPMENTS

Financial Services and Markets Act 2000 (Short Selling) Regulations 2012

On October 9, the Financial Services and Markets Act 2000 (Short Selling) Regulations 2012 (the Regulations) were published. The Regulations relate to the EU Regulation on Short Selling and Certain Aspects of Credit Default Swaps (the Short Selling Regulation). The Regulations repeal certain UK statutory and regulatory provisions which are inconsistent with the Short Selling Regulation, designate the UK Financial Services Authority (FSA) as the UK's competent authority under the Short Selling Regulation, and provide the FSA with specific powers of enforcement and investigation as well as other administrative powers with respect to matters within the scope of the Short Selling Regulation.

Read more.

EU DEVELOPMENTS

ESMA Publishes Updated Short Selling Regulation Questions and Answers

On October 10, the European Securities and Markets Authority (ESMA) published an update to its *Questions and Answers: Implementation of the Regulation on Short Selling* (the Q&A). The Q&A, originally issued on September 13 (as reported in the September 14, 2012 edition of *Corporate and Financial Weekly Digest*), addresses questions arising with respect to the implementation of the EU Regulation on Short Selling and Certain Aspects of Credit Default Swaps (the Short Selling Regulation) which comes into force on November 1. The purpose of the Q&A is to promote common supervisory approaches and practices among national securities markets regulators on the requirements of the Short Selling Regulation.

The key additions in the updated Q&A address:

- The duration adjustment formula to be used for the calculation of net short positions in sovereign debt; and
- Clarification of reporting of net short positions held by funds managed by the same manager.

Read more.

In a linked development, on October 11, ESMA published the thresholds for incremental notifications to national regulators with respect to net short positions in sovereign debt. The initial notification thresholds are: (a) 0.1% where the total amount of outstanding issued sovereign debt is 500 billion euros or less; and (b) 0.5% where the total amount of outstanding issued sovereign debt is above 500 billion euros or where there is a liquid futures market for the particular sovereign debt.

ESMA has set the thresholds for additional incremental notifications at 50% of the initial thresholds. The reporting thresholds will be monetary amounts calculated by applying the percentage thresholds to the outstanding sovereign debt of the relevant sovereign issuers. They will be revised and updated quarterly to reflect changes in the total amount of outstanding sovereign debt of each sovereign issuer.

Read more.

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