

## Corporate and Financial Weekly Digest

Business/Financial News in Brief  
**October 20, 2006**

### SEC/Corporate

#### **SEC Amends Tender Offer Best-Price Rules to Benefit Investors**

On October 18, the Securities and Exchange Commission unanimously approved changes to its “best price” rule concerning tender offers, which rule requires that all shareholders be paid the same price in a tender offer. The changes, which were a response by the SEC to conflicting court interpretations, make clear that in most circumstances compensation for services that might be paid to a shareholder is not deemed part of the price paid for such shareholder’s shares.

As amended, the tender offer best-price rules confirm that the consideration that must be paid to any security holder for securities tendered in a tender offer is the highest consideration paid to any other security holder for securities tendered in the offer. To ensure that investors are protected and the fundamental purpose of the rule is upheld, it also exempts compensatory arrangements from the rule so long as specific substantive standards are satisfied, and includes a safe harbor that hinges upon approval of independent members of the subject company’s board of directors.

“Confusion over whether compensation, severance, and other employee benefits are counted for the purpose of the best-price rule has injured investors by discriminating against tender offers,” SEC Chairman Christopher Cox said. “Our regulations should be absolutely neutral as between tender offers, mergers, and other forms of business combination so that market considerations can determine which structure creates more value for shareholders.”

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### Banking

#### **Comptroller Dugan Addresses ABA; Warns Bankers**

In prepared remarks, Comptroller of the Currency John C. Dugan cautioned bankers against easing underwriting practices and inappropriately lowering loan loss reserves during his speech on October 16 to the American Bankers Association. Mr. Dugan shared results of the interagency Shared National Credit review and the Office of the Comptroller of the Currency’s 2006 Underwriting Survey. While generally positive, this year’s SNC review showed a small decline in credit quality that followed a long period of improvement. “Even such a small decline in credit quality, however, is still a decline,” Mr. Dugan said.

“We will be monitoring whether this year’s decline portends a change in direction, or simply a stabilizing of credit quality of the syndicated loan market.” The Comptroller’s concerns about credit risk stem from the OCC’s 2006 Underwriting Survey, now in its 12<sup>th</sup> year. The survey examines 18 different product lines in the 73 largest national banks and is based on the professional opinions of OCC’s on-site examiners. “What the Underwriting Survey says this year should give us pause,” Mr. Dugan said. “Loan standards have now eased for three consecutive years.” The Comptroller reported “slippage” in commercial lending involving leverage lending and large corporate loans as well as in retail lending with significant easing in residential mortgage lending standards including home equity loans. In light of increasing credit risk, Mr. Dugan emphasized the importance of maintaining today’s strong loan loss reserves. “Solid loan loss reserves – representing the best estimate management can make of how much money the bank will lose on the loans it has made – are critical to a bank’s safety and soundness,” said the Comptroller. “That is especially true today, at a time of rising credit risk, easing underwriting standards, concentrations in some loan products, and a lack of performance experience with others.”

<http://www.occ.treas.gov/toolkit/newsrelease.aspx?Doc=S6LR4YMW.xml>

### **Office of Thrift Supervision Updates Guides for Directors**

On October 13, the Office of Thrift Supervision (OTS) issued updated versions of the Directors’ Responsibility Guide and the Directors’ Guide to Management Reports to highlight its supervisory expectations towards corporate governance practices, as well as the importance of strong, independent boards of directors. The updated Director’s Guide adds a new section on statutory and regulatory responsibility and clarifies the issue of blurred lines of responsibility between the board and management. OTS also added a chart on the applicability of selected Sarbanes-Oxley requirements.

<http://www.ots.treas.gov/docs/2/25245.pdf>

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### **Broker Dealer**

#### **NYSE Redefines “Crowd”**

The New York Stock Exchange, LLC. Market Surveillance Division released Member Education Bulletin No. 2006-20 reminding members of the revised definition of a trading crowd under NYSE Rule 70.30.

A crowd now consists of a clearly marked zone on the trading floor and trading at any panel within such zone is considered within one trading crowd. These zones were designed so that a floor broker standing within the zone is able to see and hear the business conducted at each panel within that zone. Similarly, the specialists in panels included in each zone are able to see and hear the floor brokers who are representing agency interests in that zone. The boundaries of a crowd are denoted by colored tiles mounted between the panels. A floor broker can only be in one crowd at a time.

The NYSE Market Surveillance Division reminded members that a broker who leaves one crowd to work an order in another crowd and fails to withdraw his or her agency interest is violating the rule and remains liable for any executions that take place against that interest.

[http://apps.nyse.com/commdata/PubeduMemos.nsf/AllPublishedMEBMemosNyseCom/85256F340070DCAD85257206004C175D/\\$FILE/Microsoft%20Word%20-%20Document%20in%202006-20.pdf](http://apps.nyse.com/commdata/PubeduMemos.nsf/AllPublishedMEBMemosNyseCom/85256F340070DCAD85257206004C175D/$FILE/Microsoft%20Word%20-%20Document%20in%202006-20.pdf)

## **SEC Approves Expanded OATS Requirements**

The Securities and Exchange Commission approved amendments to NASD rules expanding the Order Audit Trail System (OATS) reporting requirements to cover OTC equity securities to include those traded (i) over the counter, i.e., not on Nasdaq, (ii) on regional stock exchanges, and (iii) in direct participation programs. NASD Rules 6950 through 6957 impose obligations on member firms to record in electronic form and report to NASD on a daily basis information regarding orders originated, received, transmitted, modified, canceled or executed by members relating to equity securities. OATS captures this order information and integrates it with quote and transaction information to create a time-sequenced record of orders, quotes and transactions.

Direct purchase plans would be subject to the OATS requirements, although the NASD plans to reevaluate that requirement at a later date if necessary. The amendments will take effect six months after NASD publishes revised OATS technical specifications.

<http://www.sec.gov/rules/sro/nasd/2006/34-54585.pdf>

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## **United Kingdom Developments**

### **Bank of England Acknowledges Hedge Funds' Positive Contribution to Financial Stability**

In a major speech entitled *Hedge Funds and Financial Stability* delivered to an industry conference on October 17, Bank of England Deputy Governor, Sir John Gieve, discussed the impact of hedge funds on the financial system and considered potential risks to financial stability.

He suggested that the recent explosive growth of hedge funds was a response to technological advances and the innovation and specialization they allowed. He observed that: "In the long term that shift should be good for stability." Adding further detail, he continued: "The active trading of hedge funds makes markets more liquid and facilitates genuine hedging activity by others – including systemically important banks. Increasingly, hedge funds – led by those managed from London – have become an important part of the risk transfer process."

Sir John considered that there were risks in the short term: "Periods of rapid growth and innovation in financial markets have often led to difficulties and overshooting and we should not assume that this one will be different." He noted that "after a short pause in May and June, we have seen the return of aggressive risk taking in many financial markets this autumn."

He concluded by stating that the regulators were working with the industry to assess and mitigate the risks. He observed that the rapid growth of hedge funds was part of a wider transformation of financial markets which in the long term there were good reasons to consider welcome "not just in widening the range of options for investors but in promoting the stability of the financial system."

<http://www.bankofengland.co.uk/publications/speeches/2006/speech285.pdf>

## **FSA Consultation on Proposed Changes to the Listing and Prospectus Rules**

On October 6, the Financial Services Authority (FSA) published a consultation paper (CP06/17) on proposed changes to the Listing and Prospectus Rules. The purpose of the proposals is to address issues that have emerged since the entry into force, on July 1, 2005, of the new UK rules which implemented the EU Prospectus Directive. The FSA has stated that its aim is to deal with a number of areas where their rules may be hindering market efficiency. CP06/17 proposes changes to the procedural aspects of prospectuses, the application for listing procedure, the cancellation of listing and the application process for depositary receipts and securitised derivatives. The FSA considers that the net effect of these proposals would be deregulatory, in line with the FSA's aim of simplifying its rules and its long term objective of transforming its approach from "rules-based" to "principles-based." While the proposals in CP06/17 are relatively minor, they represent examples of the FSA's approach of working closely with market participants and co-operating with them in developing market-based solutions where possible.

[http://www.fsa.gov.uk/Pages/Library/Policy/CP/2006/06\\_17.shtml](http://www.fsa.gov.uk/Pages/Library/Policy/CP/2006/06_17.shtml)

## **FSA Issues Update on MiFID Implementation**

On October 17, the Financial Services Authority (FSA) published an update on the FSA plan for implementation of the EU Markets in Financial Instruments Directive (MiFID). The FSA set out a revised program of consultation papers and rulemaking, together with other planned publications in the run-up to transposition of MiFID (due by January 31, 2007) and implementation (due date is November 1, 2007). The MiFID-led changes to the regulatory system in the UK and the rest of Europe are enormously far-reaching and will have a significant impact on aspects of the business of every regulated investment firm.

The following papers have been issued so far and feedback on consultation responses is awaited: DP06/3: Implementing MiFID's Best Execution Requirements (May 2006); CP06/9: Organizational Systems and Controls - Common Platform for Firms (May 2006); and CP06/14 Implementing MiFID for Firms and Markets (July 2006). Two further major consultation papers are due before the end of this month: *Reforming the Conduct of Business Rules* and *Marketing Communications*.

[http://www.fsa.gov.uk/pubs/international/mifidplan\\_update.pdf](http://www.fsa.gov.uk/pubs/international/mifidplan_update.pdf)

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## **Litigation**

### **Certifications Pursuant to Sarbanes-Oxley Act Insufficient to Prove Intent to Defraud**

Putative class action lead plaintiff alleged that individual officers of the defendant corporation were liable for securities fraud in connection with various alleged accounting manipulations. The Eleventh Circuit affirmed the lower court's ruling that the plaintiff failed to plead facts sufficient to establish the strong inference of scienter needed to support the claims. Although the plaintiff alleged various accounting misrepresentations, its allegations failed to provide the type of who, what and where details needed to move beyond mere speculative and conclusory allegations that fall short of establishing scienter. Plaintiff fared no better with its alternate claim that its allegations that the individual officers signed personal certifications covering the corporation's financial statements, as required by the Sarbanes-Oxley Act, sufficiently alleged their intent to defraud. In rejecting the claim, the Eleventh Circuit held, among other things, that a personal certification is only probative of an intent to defraud if the person signing the certification knew, or was reckless in not knowing, that the financial statements covered by the

certification contained material misstatements or omissions. (*Garfield v. NDC Health Corporation*, 2006 WL 2883238 (11th Cir. Oct. 12, 2006))

### **Court Dismisses Antitrust Claim for Lack of Specific Personal Jurisdiction**

Plaintiffs alleged that defendants violated the Sherman Act and Clayton Act by tying the sale of the non-resident defendant watch company's parts to the purchase of the same company's authorized maintenance and repair services. The non-resident defendant argued that it was not subject to the court's jurisdiction because it was not responsible for the complained of practice of tying access to its replacement parts to use of its repair services. Plaintiff alleged that jurisdiction was proper because, among other things, the non-resident defendant suggested prices for its brand of watches to the resident co-defendant and because it created the illusion of one global brand through its website, which was accessible in the jurisdiction. In dismissing the claims asserted against the non-resident defendant for lack of jurisdiction, the district court explained that plaintiff must establish a causal relationship between the contacts of the non-resident and the claims at issue in order to satisfy the requirements for specific personal jurisdiction. The court found that the plaintiff failed to meet this burden both because it did not proffer facts to overcome the non-resident's showing that it had no role in the allegedly unlawful tying arrangement and because it failed to show how the non-resident's alleged in-state conduct (e.g., suggesting prices and seeking to develop a global brand) was causally related to the alleged tying arrangement. (*Fleury v. Cartier International*, 2006 WL 2934089 (N.D. Cal. Oct. 13, 2006))

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### **CFTC**

#### **CFTC Proposes to Amend Rules Relating to Filing of Regulatory Exemption Notices for CPOs and CTAs**

The Commodity Futures Trading Commission has proposed to amend its rules regarding the filing of exemption and exclusion notices under Part 4 of the CFTC's regulations, which governs the operations of commodity pool operators (CPOs) and commodity trading advisors (CTAs). Specifically, the Commission proposes to amend Rules 4.5, 4.7, 4.12, 4.13, and 4.14. Currently, notices of exemption or exclusion from the registration, recordkeeping and other provisions applicable to CPOs and CTAs under Part 4 are filed in paper form with the National Futures Association. If adopted, the amended rules would require that such notices be filed electronically with the National Futures Association. In lieu of a manual signature, the electronic notice would be required to be submitted by a representative authorized to bind the submitting party. In addition, the amended rules would expressly permit the submitting party, with the exception of "otherwise regulated" parties relying upon Rule 4.5, to electronically transmit to pool participants any required written notice of its exemption or exclusion.

The comment period closes on November 13.

<http://www.cftc.gov/files/foia/fedreg06/foi061013a.pdf>

#### **CFTC Proposes to Prospectively Supersede Advisory Regarding Disclosure, Recordkeeping and Reporting Exemptions for Offshore Commodity Pools**

In the same notice, the Commodity Futures Trading Commission has also requested comment on the continued applicability of Advisory 18-96, which provides exemptions from certain disclosure, recordkeeping and reporting requirements to the registered commodity pool operator (CPO) of a pool that is organized and operated outside of the U.S. and offered exclusively to non-U.S. persons. In the



Commission's view, Advisory 18-96 is no longer necessary, since the exemption under Rule 4.13(a)(4) already provides more extensive relief. The CFTC has asked whether requiring CPOs to file for exemption under 4.13(a)(4) rather than the Advisory might have adverse consequences that it has not identified. The CFTC emphasizes that, if it adopts this policy, its effect would be prospective only, and that CPOs who have previously claimed relief under the Advisory could continue to rely on such claim or file a claim for exemption under Rule 4.13(a)(4).

The comment period closes on November 13.

<http://www.cftc.gov/files/foia/fedreg06/foi061013a.pdf>

<http://www.cftc.gov/tm/tmcpo-adv.htm>

## **CFTC Enters into Regulatory Cooperation Arrangement with Forwards Market Commission of India**

On October 18, the Commodity Futures Trading Commission entered into an Arrangement Regarding Regulatory Cooperation and Technical Assistance with the Forward Market Commission of India, the Indian commodities regulator.

<http://www.cftc.gov/opa/press06/opa5250-06.htm>

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