

Corporate and Financial Weekly Digest



October 24, 2008

SEC/Corporate

NASDAQ Temporarily Suspends Bid Price and Market Value of Publicly Held Shares Requirements

Effective October 16, the NASDAQ Stock Market LLC temporarily suspended the bid price and market value of publicly held shares requirements for continued NASDAQ listing through January 16, 2009. NASDAQ rules require listed companies to have a minimum closing bid price of \$1.00 and a minimum market value of publicly held shares. NASDAQ acted at this time because the number of securities trading below \$1 per share increased from 64 on September 30, 2007, to 344 on October 9, 2008, without there having been a fundamental change in the business of many of these companies.

As a result of the rule suspension, all listed companies presently in the compliance process will remain at that same stage of the process. Listed companies will not be cited for new bid price or market value of publicly held share deficiencies during the suspension period, and the time allowed to listed companies already in a compliance period or in the hearings process for bid price or market value of publicly held shares deficiencies will be suspended with respect to those requirements. NASDAQ will determine any new deficiencies with the bid price or market value of publicly held shares requirements using data beginning on January 19, 2009. However, if such listed company is presently subject to being delisted for concerns not related to the bid price or market value of publicly held shares requirements, it will continue in that process with respect to those other concerns.

NASDAQ will continue to monitor listed companies to determine if they regain compliance with these requirements during the suspension period.

http://www.nasdaq.com/about/IA_2008-005.pdf

<http://www.nasdaq.com/about/SR-NASDAQ-2008-082.pdf>

Litigation

Summary Judgment to SEC Against a Broker Upheld on Appeal

The First Circuit Court of Appeals affirmed the entry of summary judgment against a broker for violating Section 10(b) of the Securities and Exchange Act and Rule 10b-5 by intentionally concealing his identity and the identities of his clients in order to mislead mutual fund companies so that they would process trades that they otherwise would not have allowed.

The Securities and Exchange Commission claimed that the broker engaged in "market timing" by taking advantage of the time zone differences between the daily closings of the foreign and U.S. markets, i.e., by making trades based on foreign market closing prices that utilize information becoming available after

SEC/CORPORATE

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the foreign market close. Although market timing is not illegal, mutual fund companies often prohibit it in order to protect their long-term shareholders and prevent stock dilution and other adverse effects. Because defendant was suspected of engaging in market timing, various mutual funds blocked him from executing trades under his financial advisor (FA) number and his customer accounts numbers. In response, defendant began using new FA and customer numbers to evade the “block” and continue to execute trades.

The district court granted the SEC’s summary judgment motion based on evidence that defendant was aware of the mutual funds’ policies prohibiting market timing, defendant’s e-mail communications with customers discussing his market timing strategies and evidencing intent to mislead the mutual funds into processing prohibited trades, and defendant’s invocation of the Fifth Amendment privilege when the SEC sought to depose him. On appeal, defendant argued that testimony he had given in SEC and National Association of Securities Dealers (NASD) investigations that preceded the SEC’s civil action against him raised a genuine issue of material fact concerning his scienter. The First Circuit rejected defendant’s argument for multiple reasons. For example, the court ruled that the defendant failed to refer to any specific testimony from the earlier SEC investigation that raised a genuine issue of material fact. Further, the court found that defendant could not rely on his NASD testimony because he had refused to answer questions about blocked account numbers in his NASD testimony and, thus, prevented the NASD from obtaining his testimony on matters that were “pertinent to [the] scienter [issue].” (*SEC v. Ficken*, 2008 WL 4615797 (1st Cir. Oct. 20, 2008))

Shareholders’ Securities Fraud Action Against Company’s Officers Dismissed

Plaintiffs alleged that defendants made false or misleading statements and omissions regarding the company’s products and partnerships in various press releases and investor conference calls during the period from 2000 to 2006 during which plaintiffs purchased company stock. For example, several of defendants’ statements in 2004 and 2005 set forth the company’s expectation that it would be entering into partnerships to exploit its Aprotinin product and generate revenue therefrom. Consistent with these statements, in November 2005 defendants announced that the company had entered into “new partnering discussions for development of [Aprotinin]” and would be completing the transaction “during the next days.” Notwithstanding this statement, the company shut down its operations one month later and filed for bankruptcy in January 2006. Following its bankruptcy filing, the company’s stock plummeted, and plaintiffs suffered close to \$900,000 in losses.

In granting defendants’ motion to dismiss, the court noted that the statements at issue, which concerned “anticipated partnership agreements, developmental research and revenue streams from product sales,” were all forward-looking statements under the Private Securities Litigation Reform Act. The court ruled that none of these statements could support plaintiffs’ Section 10(b) and Rule 10b-5 claims because plaintiffs alleged no facts indicating that (i) defendants failed to disclose the forward-looking nature of their statements when they made them, or (ii) the statements were false when made or that defendants knew that they were false when made. Plaintiffs’ conclusory allegation that the statements were false, unsupported by any specific facts, was not enough to withstand defendants’ motion to dismiss.

The court also ruled that plaintiffs’ scienter allegations were deficient because they asserted only general allegations relating to defendants’ compensation and motives for lending money to the company. Moreover, even assuming that the statements at issue were false and were made with scienter, the court ruled that plaintiffs’ claims were still defective because they had not shown that they relied on the allegedly false statements or that such statements caused their injury. The court found that plaintiffs did not tie any of their stock

purchases between 2000 and 2006 to any of the defendants' alleged false statements. Similarly, with respect to loss causation, the court ruled that plaintiffs failed to show that any of the alleged misstatements contributed to the decline in the company's stock price. (*Lory v. Ryan*, 2008 WL 4630306 (D. Ariz. Oct. 20, 2008))

Broker Dealer

CBOE Announces Intent to Launch C2 All-Electronic Exchange

The Chicago Board Options Exchange (CBOE) has announced a plan to launch a second, all-electronic options exchange tentatively called the C2 Exchange. In Information Circular IC08-175, issued October 21, the CBOE stated that the C2 Exchange is intended to complement its hybrid marketplace by extending customer reach and enhancing its competitiveness with the recently formed NYSE/PCX/AMEX and NASDAQ/PHLX combinations. CBOE plans to discuss the most attractive and competitive structure for the C2 Exchange with members and member firms, with an anticipated 2009 launch subject to regulatory approval.

<http://www.cboe.org/publish/InfoCir/IC08-175.pdf>

Structured Finance and Securitization

Fitch Announces Proposals to Revise Ratings Methodology for Structured Finance CDOs

On October 16, Fitch Ratings announced proposals to restructure its rating system for structured finance collateralized debt obligations (CDOs). The proposals expand Fitch's criteria for reviewing structured finance CDOs with exposure to U.S. subprime residential mortgage-backed securities. The previous criteria were issued in November 2007. The updated rating system, once in effect, will apply to CDOs exposed to many structured finance assets, including U.S. commercial mortgage-backed securities and European structured finance securities.

http://www.fitchratings.com/corporate/sectors/criteria_rpt.cfm?sector_flag=1&marketsector=2&detail=&body_content=crit_rpt

CRS Releases Report on the Treasury Asset Purchase Plan

On October 14, the Congressional Revenue Service released a report entitled "Auction Basics: Background for Assessing Proposed Treasury Purchases of Mortgage-Backed Securities." The report discusses the mechanisms proposed to be used by the Treasury Department in purchasing troubled assets under the Emergency Economic Stabilization Act of 2008. It covers the use of reverse Dutch auctions by the federal government and the potential design of the Treasury auction program.

http://assets.opencrs.com/rpts/RL34707_20081014.pdf

FDIC Chairman Testifies on EESA Guarantees of Modified Mortgages

On October 23, the U.S. Senate Committee on Banking, Housing and Urban Affairs held a hearing titled "Turmoil in the U.S. Credit Markets: Examining Recent Regulatory Responses." During the hearing, Sheila Bair, the Chairman of the Federal Deposit Insurance Corporation, testified that the Emergency Economic Stabilization Act of 2008 provides the authority for the government to prevent avoidable foreclosures by establishing standards for servicers to modify mortgage loans and providing guarantees or other credit enhancements for loans meeting those standards.

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Other witnesses providing testimony at the hearing included Neel Kashkari, Interim Assistant Secretary for Financial Stability and Assistant Secretary for International Affairs, U.S. Department of the Treasury; James B. Lockhart, III, Director, Federal Housing Finance Agency; Elizabeth A. Duke, Governor, Board of Governors of the Federal Reserve System; and Brian D. Montgomery, Federal Housing Commissioner and Assistant Secretary, Department of Housing and Urban Development.

<http://banking.senate.gov/public/index.cfm?Fuseaction=Hearings.Detail&Heari ngID=3df09367-cf45-438a-9c0f-7ebfec169719>

CFTC

CFTC Issues Exemption from Foreign Futures and Options Regulations

On October 14, the Commodity Futures Trading Commission granted an exemption from certain foreign futures and options regulations to firms designated by the Tokyo Financial Exchange, Inc. The exemption was issued pursuant to CFTC Regulation 30.10 and is based on substituted compliance with comparable regulatory and self-regulatory requirements of a foreign regulatory authority, consistent with conditions specified by the CFTC.

<http://www.cftc.gov/stellent/groups/public/@lrfederalregister/documents/file/e8-24315a.pdf>

CFTC Approves NFA Compliance Rules on Disclosure by Forex Pool Operators and Trading Advisors

The Commodity Futures Trading Commission has approved the National Futures Association's (NFA) Rules 2-41 and 2-42, requiring NFA members who manage customer OTC foreign currency (forex) accounts or offer pools trading forex to provide to prospective clients and pool participants a disclosure document, which must be filed with NFA prior to its first use and contain disclosures similar to those required under CFTC Part 4 regulations. In addition, a member operating a pool trading forex would be required to provide periodic (monthly or quarterly) account statements and an annual report to the pool participants. The new rules, which will become effective on November 30, will apply only if the forex pool or the customer for whom the forex account is being managed is not an "eligible contract participant" as set forth in Section 1a(12) of the Commodity Exchange Act.

<http://www.nfa.futures.org/news/newsNotice.asp?ArticleID=2191>

Banking

Fed Announces Creation of Money Market Investor Funding Facility To Bolster Money Market Mutual Funds

The Federal Reserve Board announced on October 21 the creation of the Money Market Investor Funding Facility (MMIFF), which will support a private-sector initiative designed to provide liquidity to U.S. money market investors. Under the MMIFF, authorized by the Board under emergency provisions of the Federal Reserve Act, the Federal Reserve Bank of New York will provide senior secured funding to a series of special purpose vehicles to facilitate an industry-supported private-sector initiative to finance the purchase of eligible assets from eligible investors. Eligible assets will include U.S. dollar-denominated certificates of deposit and commercial paper issued by highly rated financial institutions and having remaining maturities of 90 days or less. Eligible investors will include U.S. money market mutual funds and over time may include other U.S. money market investors.

CFTC

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The linked term sheet describes the basic terms and operational details of the facility.

The MMIFF complements the previously announced [Commercial Paper Funding Facility](#) (CPFF), which on October 27 will begin funding purchases of highly rated, U.S. dollar-denominated, three-month, unsecured and asset-backed commercial paper issued by U.S. issuers, as well as the [Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility](#) (AMLF), announced on September 19, which extends loans to banking organizations to purchase asset-backed commercial paper from money market mutual funds. The AMLF, CPFF, and MMIFF are all intended to improve liquidity in short-term debt markets and thereby increase the availability of credit.

http://www.newyorkfed.org/markets/mmiff_terms.html

http://www.newyorkfed.org/markets/mmiff_faq.html

Federal Reserve Eases Usual Restrictions on Preferred Stock to Be Purchased by Treasury

The Federal Reserve Board announced on October 16 the adoption of an interim final rule that will allow bank holding companies to include in their Tier 1 capital without restriction the senior perpetual preferred stock issued to the Treasury Department under the capital purchase program announced by the Treasury on October 14. Treasury established the capital purchase program under the Emergency Economic Stabilization Act of 2008, which became law on October 3. Certain features of the preferred stock as proposed by Treasury, such as the step up in rate from five to nine percent after five years, would normally have prevented the preferred shares from counting as Tier 1 capital.

The interim rule will be effective as of October 17. The Board is, however, seeking public comment on the interim rule. Comments must be submitted by November 21.

<http://www.americanbanker.com/media/regulatory/federalregister/pdfs/102208.pdf>

UK Developments

FSA Amends Short Selling Daily Disclosure Requirement

On October 22, the UK Financial Services Authority (FSA) announced that it had completed its 30-day review of the additional short selling provisions introduced to its Code of Market Conduct on September 18, 2008 (as reported in the September 19, 2008 edition of [Corporate and Financial Weekly Digest](#)).

The FSA has decided to make only one change. It will amend the Code of Market Conduct so that once disclosure of a short position has been made, additional disclosures will only be required when that short position changes, not, as currently required, on a daily basis. The FSA will make a further announcement once the change has been made.

www.fsa.gov.uk/pages/Library/Communication/PR/2008/122.shtml

FSA Gives Feedback on Disclosure of Contracts for Difference (CFDs)

On October 23, the UK Financial Services Authority (FSA) published a feedback statement on proposals for the disclosure of long positions held as contracts for difference (CFDs) set out in its consultation paper published in November 2007 (as reported in the November 16, 2007 edition of [Corporate and Financial Weekly Digest](#)). The FSA has announced that it will implement a

UK DEVELOPMENTS

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general disclosure regime for long CFD positions. The initial disclosure threshold will be at 3%, in line with the existing UK disclosure rules for positions in equity securities. The FSA proposes to exempt CFD writers which act as intermediaries in order to reduce unnecessary disclosures. The feedback statement contains draft rules, and the FSA will accept technical comments on the rules until January 23, 2009. The FSA expects to issue final rules in February 2009 which will come into effect September 1, 2009.

www.fsa.gov.uk/pubs/cp/cp08_17.pdf

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