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CORPORATE & FINANCIAL
WEEKLY DIGEST

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SEC/CORPORATE

SEC Will Not Appeal Proxy Access Decision; Rule 14a-8 Amendment To Become Effective

Mary Schapiro, Chairman of the Securities and Exchange Commission, announced this week that the SEC will not appeal the decision of the U.S. Court of Appeals for the District of Columbia's decision vacating SEC Rule 14a-11, which would have required companies to include shareholders' director nominees in company proxy statements. In her announcement, SEC Chairman Schapiro stated that the SEC will continue to seek to provide "a meaningful opportunity for shareholders to exercise their right to nominate directors" and is analyzing the U.S. Court of Appeal's objections and continuing to review comments previously received on Rule 14a-11.

Pending the U.S. Court of Appeals decision, the SEC had stayed the effective date of Rule 14a-11 along with a companion amendment to Rule 14a-8, the shareholder proposal rule. Under the latter rule amendment, eligible shareholders are permitted to require companies to include shareholder proposals regarding proxy access procedures in a company's proxy materials. In announcing that the SEC would not appeal the Rule 14a-11 decision, Chairman Schapiro also announced that the Rule 14a-8 amendment will be permitted to go into effect and that notice of the effective date of the amendment, presumably September 13, will be published by the SEC.

To view SEC Chairman Mary Schapiro's statement, click here.

SEC Lowers Listing Fees for Fiscal Year 2012

Effective October 1, the fees that public companies and other issuers pay to register their securities with the Securities and Exchange Commission will decrease from $116.10 per million dollars to $114.60 per million dollars. This fee rate is applicable to the registration of securities under Section 6(b) of the Securities Act of 1933, the repurchase of securities under Section 13(e) of the Securities Exchange Act of 1934, and proxy solicitations and statements in corporate control transactions under Section 14(g) of the Exchange Act.

Click here for the SEC's fee rate advisory.

SEC Recoups Bonus of Former Beazer Executive Under Sarbanes-Oxley

On August 30, the Securities and Exchange Commission announced a settlement with the former chief financial officer of Beazer Homes USA to recover more than $1.4 million in bonus and stock profits that he received after the home builder filed fraudulent financial statements during fiscal year 2006.

Although the chief financial officer, James O'Leary, was not himself charged with wrongdoing, the SEC claimed in its complaint that it was required under Section 304 of the Sarbanes-Oxley Act to recoup the money on behalf of Beazer. The SEC argued that money can be recouped based on required certifications that O'Leary made pursuant to Section 302 of the Sarbanes-Oxley Act in Beazer's quarterly and annual reports concerning the accuracy of Beazer's financial statements. The SEC's settlement with O'Leary is subject to court approval.

Section 304 requires reimbursement to the company by the chief executive officer (CEO) and chief financial officer (CFO) of the issuer for incentive or equity-based compensation received during the 12-month period following the issuance of restated financial statements where there is "material noncompliance of the issuer, as a result of misconduct," with financial reporting requirements. In this instance, such compensation included O'Leary's bonuses and equity-based compensation, as well as the profits he received from selling Beazer stock he received on exercise of stock options.

This is only the second time the SEC has succeeded in enforcing its interpretation of Section 304 to apply to a CEO or CFO even though the executive officer was not accused of engaging in "misconduct."

To read the SEC press release announcing this settlement, click here.

BROKER DEALER

SEC Seeks Review of Existing Regulations

On September 6, the Securities and Exchange Commission announced that it is seeking public comment on the development of a plan for the retrospective review of its regulations. Executive Order 13579 signed by the President on July 11, requires independent agencies to "develop and release to the public a plan...under which the agency will periodically review its existing significant regulations." In response to the Executive Order and its continuing efforts to update its regulations to reflect market developments and changes in the regulatory landscape, the SEC invites public comments on the development of its plan for retrospective review. Public comments must be submitted by October 6.

Click here to read SEC Release No. 32-9257.

CFTC

CFTC Allows U.S. Trading of Euronext Brussels' Futures Contract on BEL 20 Index

On August 31, the Commodity Futures Trading Commission's Office of General Counsel issued a no-action letter allowing the offer and sale in the U.S. of the BEL 20 Index futures contract that is traded on Euronext Brussels.

A copy of the no-action letter may be found here.

CFTC Grants CME Clearing Europe Limited Registration as a Derivatives Clearing Organization

On September 2, the Commodity Futures Trading Commission issued an order granting CME Clearing Europe Limited registration as a derivatives clearing organization pursuant to Section 5b of the Commodity Exchange Act. Under the terms of the order, CME Clearing Europe Limited is permitted to clear swaps and forward contracts on energy, agricultural, freight and metals products executed either bilaterally or on or through a swap execution facility.

A copy of the Order of Registration may be found here.

INVESTMENT COMPANIES AND INVESTMENT ADVISORS

SEC Issues Concept Releases on Investment Company Derivative Use, Mortgage Securities and Rule 3a-7

On August 31, the Securities and Exchange Commission issued three concept releases regarding: (i) the use of derivatives by investment companies (Derivatives Release), (ii) companies engaged in the business of acquiring mortgages and mortgage-related instruments (Mortgage Securities Release), and (iii) the treatment of asset-backed issuers under Rule 3a-7 (Rule 3a-7 Release). In the concept releases, the SEC requests comments from the public on a variety of issues. Comments for all of the concept releases should be received on or before November 7.

Derivatives Release. The SEC and its staff are reviewing the use of derivatives by management investment companies registered under the Investment Company Act of 1940 (the 1940 Act), including exchange-traded funds (ETFs) as well as business development companies (collectively, Funds). In the Derivatives Release, the SEC requests comments on a range of issues, including potential implications for Fund leverage, portfolio concentration, diversification, valuation, exposure to securities-industry issuers, collateralization, counterparty risk and related matters. Comments received by the SEC will be used to determine whether regulatory initiatives or guidance are needed to improve the current regulatory regime for Funds and, if so, the nature of any such initiatives or guidance. Separate from the Derivatives Release, the SEC is presently examining the impact of leveraged and inverse ETFs, which rely heavily in derivatives in order to obtain their investment objectives, on market volatility in August 2011.

Mortgage Securities Release. Under the Mortgage Securities Release the SEC is reviewing the status of companies under the 1940 Act, such as real estate investment trusts, that are engaged in the business of acquiring mortgages and mortgage-related instruments and that rely on Section 3(c)(5)(C) of the 1940 Act for an exclusion from the definition of investment company (together, Mortgage Pools). To facilitate the review, the SEC is requesting information about such companies and how Section 3(c)(5)(C) is interpreted by, and affects investors in, such companies. The SEC is also requesting commenters' views on the application of the 1940 Act to Mortgage Pools, including suggestions on steps that the SEC should take to provide greater consistency, regulatory certainty, or clarity with respect to Section 3(c)(5)(C).

Rule 3a-7 Release. The SEC is considering proposals to amend Rule 3a-7 under the 1940 Act. Rule 3a-7 provides certain asset-backed securities issuers with a conditional exclusion from the definition of investment company. The SEC is requesting commenters' views on potential amendments and considerations to reflect market developments since 1992 (the year that Rule 3a-7 was adopted); recent developments affecting asset-backed issuers, including the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act and the SEC's recent rulemakings regarding asset-backed securities markets; and the role, if any, that credit ratings should continue to play in the context of Rule 3a-7. In the Rule 3a-7 Release, the SEC also withdrew its 2009 proposal to amend Rule 3a-7, which was published at 73 FR 40124 on July 11, 2008.

Click here to read the Derivatives Release (Release No. IC-29776).

Click here to read the Mortgage Securities Release (Release No. IC-29778).

Click here to read the Rule 3a-7 Release (Release No. IC-29779).

LITIGATION

Third Circuit Affirms District Court's Dismissal of Securities Fraud Class Action for Failure to Plead Scienter

The U.S. Court of Appeals for the Third Circuit affirmed the District Court's grant of defendants' motion to dismiss all claims against corporate defendants and individual officers and directors of Horizon Lines, Inc. for securities fraud arising out of price fixing under the heightened pleading standard in the Private Securities Litigation Reform Act (the PSLRA). Highlighting that the PSLRA places a weighty burden on plaintiffs, the Third Circuit affirmed that plaintiff did not plead sufficient facts to raise a strong inference of scienter as to the senior executives of Horizon. The Third Circuit further held that in pleading scienter as to the corporation, one still needed to look to the state of mind of the individual corporate officials who made the statements at issue, as opposed to the collective knowledge of all the corporation's employees. Because there was no individual at Horizon who made actionable statements with scienter, the Third Circuit affirmed the District Court's determination that the plaintiff had not pled scienter against the corporation.

City of Roseville Employees' Retirement System v. Horizon Lines, Inc., Nos. 10-2788 and 10-3815 (3d Cir. Aug. 24, 2011).

Defendants' Ineffective Document Review Procedure Results in Finding of Waiver

The U.S. District Court for the Northern District of Illinois held that defendants, Village of Park Forest and individual defendants (collectively, the Village), waived privilege as to inadvertently produced documents where they failed to take reasonable precautions to prevent the disclosure of privileged material and subsequently failed to correct their error in a timely manner. Citing defendants' lack of an adequate explanation of their review process, their failure to check the production before sending it to the plaintiffs and their ultimate failure to identify and withhold from production any of the 159 documents on their privilege log, the court determined that the steps taken to prevent disclosure were not reasonable. Further, the Court found no unfairness in allowing the plaintiffs to access the privileged documents and ultimately held the Village responsible for its failure to take reasonable care to safeguard the privilege and to rectify the error once it occurred.

Thorncreek Apartments III, LLC v. Village of Park Forest, et al., Nos. 08 C 1225, 08 C-0869, 08-C-4303 (N.D. Ill. Aug. 9, 2011).

Creditors of Insolvent Limited Liability Companies Cannot Sue Derivatively

The Supreme Court of Delaware recently held that creditors of insolvent Delaware limited liability companies (LLCs) lack standing to bring derivative suits on behalf of the LLCs.

In March 2010, CML V brought both derivative and direct claims against the present and former managers of JetDirect Aviation Holdings LLC in the Court of Chancery after JetDirect defaulted on its loan obligations to CML. The Vice Chancellor dismissed all the claims, finding that, as a creditor, CML lacked standing to bring derivative claims on behalf of JetDirect, and CML appealed.

The Supreme Court affirmed the Vice Chancellor's decision, holding that Sections 18-1001 and 18-1002 of the Delaware Limited Liability Company Act (LLC Act) conclusively establish that only members or assignees of an LLC may sue derivatively in the name of the company. In doing so, the Court rejected CML's argument that creditors of insolvent LLCs should be treated similarly to creditors of insolvent corporations, pointing out that the plain language of the LLC Act precluded such a result. In addition, the Supreme Court further rejected CML's argument that the denial of standing to creditors was an unconstitutional limitation on the Court of Chancery's powers "in equity."

CML V, LLC v. Bax, No. 735, 2010 (Del. Sept. 2, 2011, corrected on Sept. 6, 2011).

Seventh Circuit Cuts Damages Award Due to Lack of Evidence of Lost Profits

The U.S. Court of Appeals for the Seventh Circuit dramatically reduced damages awarded to a defunct internet marketing company, finding that the company squandered its opportunity to provide a reasonable estimate of the harm it suffered as a result of the defendant's conduct.

e360 Insight, Inc. (e360) sued the Spamhaus Project, a British nonprofit, in 2006. e360 accused Spamhaus of tortious interference and defamation arising out of Spamhaus' addition of e360 to its list of known spammers. e360 initially obtained a default judgment against Spamhaus in a district court in Illinois. The District Court also awarded e360 damages of $11,715,000 based on an affidavit from e360's founder. The Seventh Circuit vacated the damages award and remanded the matter for further inquiry as to the extent of damages suffered by e360. After a bench trial on the damages issue, the District Court lowered e360's damages to $27,002: $27,000 for its tortious interference with contractual relations claim and nominal damages of $1 each on its tortious interference with prospective economic advantage and defamation claims. Both parties appealed, with Spamhaus arguing that the damages award was too high, and e360 arguing that it was too low.

The Seventh Circuit sided with Spamhaus, and vacated the $27,000 award on the tortious interference claim, ruling that the District Court erred by basing the award on lost revenues instead of lost profit. At trial, after the imposition of numerous discovery sanctions, e360 merely offered evidence of the revenues it purportedly lost. e360 presented no evidence of the costs it would incur in order to collect those revenues, making it impossible to determine e360's lost profits. The Seventh Circuit held that the failure to provide evidence of these costs "doom[s] the damage award" and vacated it, holding that e360 was only entitled to nominal damages of $1 on each of its three claims.

e360 Insight, Inc., et al. v. The Spamhaus Project, Nos. 10-3538 & 10-3539 (7th Cir. Sept. 2, 2011).

BANKING

Federal Reserve Proposes Rule to Allow Companies to Register As Securities Holding Companies

The Federal Reserve Board (the Board) on August 31 issued a proposed rule to implement Section 618 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act), which permits (but does not require) nonbank companies that own or are owned by a registered securities broker or dealer to register with the Board and subject themselves to supervision by the Board. The proposed rule outlines the requirements that a securities holding company must satisfy to make an effective registration election, including filing the appropriate form with the responsible Federal Reserve Bank. The utility of the proposed rule appears to be limited to those companies that are required by a foreign regulator or provision of foreign law to be subject to comprehensive consolidated supervision. According to the Board, only a handful of companies are expected to make an election to register, thereby subjecting themselves to extensive regulation akin to that imposed on bank holding companies (including capital requirements), but absent restrictions on non-banking activities.

To view the proposal, click here.

Federal Reserve Announces Public Hearings of Capital One Notice to Acquire ING Bank, Sharebuilder Advisors, and ING Direct Investing

The Federal Reserve Board on August 31 announced the location for a public meeting in Washington, D.C., on the notice by Capital One Financial Corporation, McLean, Virginia, to acquire ING Bank, Wilmington, Delaware, and indirectly to acquire shares of Sharebuilder Advisors, LLC, and ING Direct Investing, Inc., both of Seattle, Washington.

The public meeting in Washington will be held on Tuesday, September 20,, at the Renaissance Hotel, 999 Ninth Street, NW, Washington, D.C., and will begin at 8:30 a.m. EDT. Additional meetings will be held in Chicago on Tuesday, September 27, beginning at 8:30 a.m. CDT, at the Federal Reserve Bank of Chicago, and in San Francisco on Wednesday, October 5, beginning at 8:30 a.m. PDT, at the Federal Reserve Bank of San Francisco.

Live webcasts of the meetings will be available on the Board's website and here.

To view the Federal Reserve Board's press release, click here.

FDIC Announces New Investor Match Program

The Federal Deposit Insurance Corporation (FDIC) on September 7 announced the launch of a new program to encourage small investors and asset managers to partner with larger investors to participate in the FDIC's structured transaction sales for loans and other assets from failed banks. The Investor Match Program will help to facilitate partnerships in order to bring together sources of capital and expertise. Participants in the program will use a customized database to identify potential collaborations, which will be identified at the sole discretion of the participating firms.

The FDIC believes in the value of facilitating a cooperative solution between large investors and small investors and asset managers. The goal of the Investor Match Program is to expand opportunities for participation by smaller investors and asset managers, including minority and women-owned firms, in FDIC structured sales transactions. To participate in the Investor Match Program, every investor must be pre-qualified to bid in FDIC structured sales transactions.

The FDIC's structured transactions are one of several strategies used to sell assets retained from failed banks. Loans and real estate are transferred to a limited liability company (LLC). The FDIC then sells an equity stake in the LLC to an investor. The investor is responsible for managing the LLC and working the assets to maximize their value. This technique allows the FDIC to capture potential future upside from the assets. The dollar amount of the assets sold range from several hundred million to well over one billion dollars.

For more information on the Investor Match Program, click here.

FDIC to Hold Open Meeting on Rate Adjustments

The Board of the Federal Deposit Insurance Corporation (FDIC) will meet on Tuesday, September 13, at 10:00 a.m. in Washington, D.C., to consider assessment rate adjustments for large and highly complex financial institutions. The FDIC originally published its proposed rate adjustment guidelines on April 15.

To view the previously published proposed rate adjustment guidelines, click here.

INTELLECTUAL PROPERTY

Congress Passes Patent Reform Bill

On September 8, the Senate passed the America Invents Act (H.R. 1249) (the Act), culminating a six-year debate on patent reform in the United States. The passage of the Act represents the first reform to the United States patent system in more than 50 years and ushers in a number of significant changes that impact patent prosecution and litigation alike.

More information on the Act can be found in the September 9, 2011, Katten Client Advisory.

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