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CFTC

CFTC Issues Interpretation of "Actual Delivery"

On August 23, the Commodity Futures Trading Commission issued an interpretation of the phrase "actual delivery" as it relates to the CFTC's jurisdiction over retail commodity transactions. Section 2(c)(2) of the Commodity Exchange Act (CEA) grants the CFTC jurisdiction over retail commodity transactions, which are effectively defined as any agreement, contract or transaction in any commodity that is entered into with, or offered to, a person that is not an eligible contract participant or eligible commercial entity on a leveraged, margined or counterparty-financed basis. The CEA provides an exception for contracts that result in actual delivery within 28 days.

The interpretive statement indicates that the CFTC will employ a functional approach to determining whether a particular contract, agreement or transaction is actually delivered. The CFTC stated that, instead of relying solely upon the language used by the parties, it will examine how an agreement, contract or transaction is marketed, managed and performed by considering the following factors: ownership, possession, title and physical location of the commodity purchased or sold, both before and after execution, including all related documentation; the nature of the relationship between the buyer, seller and possessor of the commodity purchased or sold; and the manner in which the purchase or sale is recorded and completed.

The CFTC's interpretation is available here.

LITIGATION

SEC Requires Admission of Wrongdoing as Part of Settlement

Reversing its longstanding policy, the Securities and Exchange Commission recently required hedge-fund adviser Philip Falcone and his firm Harbinger Capital Partners LLC (Harbinger) to admit multiple acts of misconduct in order to settle two enforcement actions filed last year.

In papers filed in the US District Court for the Southern District of New York, the SEC alleged, and Falcone and Harbinger admitted, that: (i) Falcone improperly borrowed over $113 million from a Harbinger fund to pay his personal taxes, and did so at a preferential interest rate and despite his refusal to honor other investors' redemption requests, and then failed to disclose the transaction for five months; (ii) Falcone and Harbinger favored certain investors over others, and did not disclose such preference to the board or other investors; and (iii) in 2006, Falcone and Harbinger engaged in an illegal "short squeeze" of a certain company's bonds to punish a financial services firm.

As part of the settlement, Harbinger must pay a $6.5 million penalty. Falcone must pay approximately $6.5 million in disgorgement, $1 million in prejudgment interest and a $4 million penalty. He also agreed to be barred from the securities industry for at least five years.

Previously, the SEC permitted defendants to settle cases while still denying any wrongdoing. Thus, the Falcone and Harbinger settlement, with its numerous and specific admissions, marks a policy shift that raises several important questions. For example, as discussed elsewhere, such admissions may expose defendants to criminal liability. *See* Kurt Orzeck, "Falcone's SEC Admission Leaves Criminal Charges Up in Air." How the SEC and the Department of Justice will coordinate the prosecution of those accused of securities violations remains to be seen.

SEC v. Falcone et al., Case No. 12-cv-5027 (PAC) (S.D.N.Y. Aug. 19, 2013); *SEC v. Harbinger Capital Partners LLC et al*., Case No. 12-cv-5028 (PAC) (S.D.N.Y. Aug. 19, 2013).

SEC Accuses Investment Adviser of Misrepresenting Its Algorithmic Trading Capacity

The Securities and Exchange Commission recently charged a North Carolina-based investment adviser and its former owner with making false statements about the firm's ability to engage in algorithmic currency trading.

To procure a contract to manage a $17 million mutual fund, Elliott Shifman, the former owner of Chariot Advisors LLC (Chariot), allegedly told the fund's board at two presentations in 2008 and 2009 that Chariot had a proprietary algorithm to trade in currencies. At the time of these statements, however, Chariot did not possess such capacity, and instead relied on an individual trader who used technical analysis combined with "her own intuition." After two months, Chariot terminated this trader for poor performance and subsequently employed a third party that did use a computer algorithm to trade currency.

Although Shifman's representations as to Chariot's algorithmic trading ultimately became true, the SEC has taken a hard line with respect to false statements made during the "15(c) process." This process refers to the section of the Investment Company Act of 1940 that requires investment advisers to provide a registered fund's board with all information necessary to evaluate the fund's advisory agreements.

The Chariot investigation, which resulted in the recently filed civil administrative proceeding, is the latest development in an initiative by the SEC's Asset Management Unit to police interactions between funds and their advisers, and suggests that the 15(c) process will continue to be one of the agency's priorities.

In the Matter of Chariot Advisors, LLC and Elliott L. Shifman, A.P. No. 3-15433 (Aug. 21, 2013).

EXECUTIVE COMPENSATION AND ERISA

IRS Will Recognize All Marriages of Same-Sex Couples if Valid Where Performed

On June 26, the US Supreme Court required the federal government to recognize marriages between two individuals of the same sex if the marriage is recognized by the state in which the couple lives.

On August 29, in applying the Supreme Court's decision, the Internal Revenue Service ruled that the determination of whether a couple is married for federal tax purposes will be based on whether the marriage was legal where it was performed. By adopting the so-called "state of celebration" rule (rather than the so-called "state of domicile" rule), the IRS has made the federal tax benefits of marriage available to all same-sex couples in the United States who have chosen to marry, even if they live in states that do not currently recognize marriage equality. The ruling makes clear that marriages validly performed in any domestic or foreign jurisdiction will be recognized for federal tax purposes, but same-sex and opposite-sex couples who have only entered into civil unions, domestic partnerships or other relationships treated as equivalent to marriage will not be recognized as married for federal tax purposes.

While the IRS ruling may arguably be more broad than required by the Supreme Court's holding, the IRS found it was necessary to provide for uniform nationwide rules which are essential to efficient and fair tax administration.

The IRS ruling has a broad impact on same-sex couples who have married. It also has a potentially broad impact on employers and their benefit plans. While questions about benefit plan administration remain, some things are clear based on the IRS ruling:

- An employee who currently elects health plan coverage for a same-sex spouse and the spouse's children should no longer need to pay taxes on the value of such coverage.
- An employer who provides health plan coverage to same-sex spouses and their children should no longer need to impute income to the employees for the value of such coverage.
- For any tax year that remains open (likely tax years 2010, 2011 and 2012, and perhaps 2009), taxpayers can file refunds for overpaid employment and income taxes based on the value of same-sex spousal coverage (although an employee's amended tax return cannot limit the amendment to the overpayment related to the health plan coverage—the entire return will need to be recomputed on a "married filing separately" or "married filing jointly" basis).

While not addressed in the IRS ruling, it is arguable based on both the Supreme Court's holding and the IRS ruling that any sponsor of a self-insured group health plan may risk discrimination-based lawsuits if such plan does not either eliminate all spousal coverage or extend spousal coverage to include same-sex spouses. This may be the case regardless of whether the plan is maintained by an employer in a state that recognizes marriages between individuals of the same sex.

From a retirement plan perspective, the ruling seems to require that spousal rights under retirement plans (e.g., survivor annuities and default beneficiary designation) will apply to all married same-sex couples.

The ruling states that it is effective on a prospective basis on and after September 16, 2013 (although it may be relied on earlier for certain purposes). It also provides that additional guidance will be issued to address specific questions about benefit plan administration and the retroactive application of the Supreme Court's holding, although the ruling included no indication about the timing of future guidance or the topics that are expected to be covered.

The ruling is available here.

For more information, contact:

FINANCIAL SERVICES

Janet M. Angstadt	312.902.5494	janet.angstadt@kattenlaw.com
Henry Bregstein	212.940.6615	henry.bregstein@kattenlaw.com
Wendy E. Cohen	212.940.3846	wendy.cohen@kattenlaw.com
Guy C. Dempsey Jr.	212.940.8593	guy.dempsey@kattenlaw.com
Kevin M. Foley	312.902.5372	kevin.foley@kattenlaw.com
Jack P. Governale	212.940.8525	jack.governale@kattenlaw.com
Arthur W. Hahn	312.902.5241	arthur.hahn@kattenlaw.com
Carolyn H. Jackson	44.20.7776.7625	carolyn.jackson@kattenlaw.co.uk
Kathleen H. Moriarty	212.940.6304	kathleen.moriarty@jkattenlaw.com
Ross Pazzol	312.902.5554	ross.pazzol@kattenlaw.com
Kenneth M. Rosenzweig	312.902.5381	kenneth.rosenzweig@kattenlaw.com
Fred M. Santo	212.940.8720	fred.santo@kattenlaw.com
Christopher T. Shannon	312.902.5322	chris.shannon@kattenlaw.com
Peter J. Shea	212.940.6447	peter.shea@kattenlaw.com
James Van De Graaff	312.902.5227	james.vandegraaff@kattenlaw.com
Robert Weiss	212.940.8584	robert.weiss@kattenlaw.com
Gregory E. Xethalis	212.940.8587	gregory.xethalis@kattenlaw.com
Lance A. Zinman	312.902.5212	lance.zinman@kattenlaw.com
Krassimira Zourkova	312.902.5334	krassimira.zourkova@kattenlaw.com

LITIGATION

Tenley Mochizuki	212.940.8568	tenley.mochizuki@kattenlaw.com
Michael M. Rosensaft	212.940.6631	michael.rosensaft@kattenlaw.com

EXECUTIVE COMPENSATION AND ERISA

Daniel B. Lange	312.902.5624	daniel.lange@kattenlaw.com
Christopher K. Buch	312.902.5509	christopher.buch@kattenlaw.com

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Katten Muchin Rosenman LLP www.kattenlaw.com

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